Review of New York City's Financial Plan For Fiscal Years 2005 Through 2008

July 2004

Report 5-2005

New York State
Office of the State Comptroller
Alan G. Hevesi

Office of the State Deputy Comptroller
for the City of New York
Kenneth B. Bleiwas

Additional copies of this report
may be obtained from:

Office of the State Comptroller
New York City Public Information Office
633 Third Avenue
New York, NY 10017

Telephone: (212) 681-4824

Or through the Comptroller's website at: www.osc.state.ny.us

To help reduce printing costs, please notify the Office of the State Deputy Comptroller at (212) 383-3916 if you wish to have your name removed from our mailing list or if your address has changed.

Contents

I. Executive Summary 1

II. Economic Overview 5

III. Fiscal Year 2004 7

A. Revenue Changes 7
B. Expenditure Changes 9
C. Other Changes 10

IV. Balancing the FY 2005 Budget 11

A. Agency Actions 12
B. State Actions 12
C. Federal Actions 14
D. Tax Reduction Program 14
E. Pay-As-You-Go Capital Financing 16

V. Revenue and Expenditure Trends 17

A. Revenue Forecasts 18
1. Tax Revenues 19
2. Miscellaneous Revenues 22

B. Expenditure Forecasts 23
1. Personal Service Costs 24
2. Debt Service 30
3. Medical Assistance 31
4. Public Assistance 32
5. Judgments and Claims 33
6. Uniformed Agency Overtime 34

VI. Semi-Autonomous Agencies 37

A. Department of Education 37
B. Health and Hospitals Corporation 40
C. New York City Transit Authority 41
D. Off-Track Betting Corporation 43
E. New York City Housing Authority 45
F. Municipal Assistance Corporation 46
G. New York City Transitional Finance Authority 47
H. TSASC Inc. 47
I. New York City Municipal Water Finance Authority 48
J. Hudson Yards Infrastructure Corporation 49
K. New York Convention Center Development Corporation 51

Appendix A: Nonrecurring Resources in Fiscal Year 2005 55
Appendix B: City-Funded Staffing Levels 56

I. Executive Summary

On June 29, 2004, the City of New York submitted to the Financial Control Board a modification to its FY 2004 financial plan and a new four-year financial plan for fiscal years 2005 through 2008 (see Table 1). Although the City projects a surplus of $1.9 billion for FY 2004 and a balanced budget for FY 2005, the June Financial Plan projects large out-year budget gaps.

The City expects to end FY 2004 with a surplus of $1.9 billion, even though expenses were higher than anticipated, because revenue collections will exceed the estimates in the adopted budget by $2.4 billion—owing largely to increased Wall Street activity and real estate–related transactions. Wall Street profits totaled $16.8 billion in calendar year 2003—more than twice the 2002 level and second only to the record set in 2000. Unexpected improvement in the economy, combined with assistance from the federal and State governments, helped the City close its largest budget gap since the 1970s.

The June Plan shows large out-year budget gaps because the FY 2005 budget is balanced with $3.6 billion in nonrecurring resources (three times the FY 2004 level); because temporary taxes approved by the State last year are scheduled to be phased out; and because nondiscretionary spending continues to grow rapidly. Nondiscretionary spending is projected to increase by $4 billion, or 24 percent, between fiscal years 2004 and 2006. Pension contributions alone are projected to rise by 73 percent, or $1.7 billion, and Medicaid is projected to rise by 17 percent over the two-year period. City-funded spending, both discretionary and nondiscretionary, is projected to increase by 14 percent during the two-year period, while revenues are projected to rise by only 0.2 percent.

Consequently, the June Plan projects budget gaps of $3.7 billion in FY 2006 (11.7 percent of City fund revenues); $4.5 billion in FY 2007; and $3.7 billion in FY 2008. Our review has identified budget risks that have a net value of $623 million in FY 2005 and average $1.2 billion in subsequent years (see Table 2). While these risks should not interfere with the City's ability to maintain budget balance during FY 2005 because of the availability of reserves and other resources, they could widen the large out-year gaps projected by the City. Most of the uncertainty involves State actions and future collective bargaining costs, but we also remain concerned that rising interest rates and large federal deficits will put a damper on future economic activity.

Should these risks materialize, the gaps could reach $4.7 billion in FY 2006, $5.8 billion in FY 2007, and $5.1 billion in FY 2008. In addition, the June Plan makes no provision for wage increases during these years. Wage increases at the projected inflation rate would widen the budget gaps by $220 million in FY 2006, $700 million in FY 2007, and $1.2 billion in FY 2008.

One of the largest budget risks in the June Plan is the assumption that the State will increase gap-closing aid to the City by $400 million annually. While the City will probably receive some increase, the amount and form is not yet known because a new State budget is more than three months overdue. In addition, the Court of Appeals ruled last year that the State education aid formula shortchanges New York City and other school districts with high concentrations of low-performing students, and set a July 30 deadline for reforms. The Governor and the State's two legislative leaders have yet to agree on a new funding formula, but they agree that the City should increase its own funding for education as part of an overall settlement.

Also, the June Plan assumes that the recent collective bargaining agreement with District Council 37, which covers fiscal years 2003 through 2005, will set the pattern for contracts with other municipal unions. Applying the terms of the agreement to the unions that represent teachers and uniformed employees, however, could prove challenging.

Our review also found that the Metropolitan Transportation Authority, the Off-Track Betting Corporation, the Health and Hospitals Corporation, and the New York City Housing Authority face serious fiscal challenges. The MTA projects large funding gaps in both its operating and capital financial plans; OTB will likely end FY 2004 with a loss of $7.6 million, its first loss in a decade; HHC projects a $235 million budget gap for FY 2005 despite a $200 million increase in City support; and the Housing Authority is attempting to close a projected budget gap of $300 million by reducing staffing by 1,000 employees and by deferring maintenance.

In conclusion, the June Plan projects large out-year budget gaps because the City has yet to address the underlying imbalance between recurring revenues and expenditures and, instead, has relied on nonrecurring resources to balance the FY 2005 budget. Moreover, our review has identified a number of substantial budget risks that could widen the already large out-year budget gaps. Though the City should be commended for setting aside $220 million of the FY 2004 surplus for use in FY 2006 and for paying down $200 million of high coupon bonds due in FY 2006, the City needs to begin the process of identifying recurring actions to close the FY 2006 budget gap and to narrow the large gaps projected for subsequent years.

Table 1
Four-Year Financial Plan
(in millions)

	FY 2005	FY 2006	FY 2007	FY 2008
REVENUES				
Taxes				
General Property Tax	$11,800	$ 12,263	$ 12,807	$ 13,374
Other Taxes[1]	15,053	14,895	15,329	16,154
Tax Audit Revenue	508	508	509	509
Tax Program	(300)	(305)	(310)	(64)
Miscellaneous Revenue	5,784	4,279	4,231	4,264
Unrestricted Governmental Aid	562	562	562	562
Anticipated State and Federal Aid	450	400	400	400
Less: Intra-City Revenues	(1,146)	(1,131)	(1,130)	(1,130)
Grant Disallowances	(15)	(15)	(15)	(15)
Subtotal: City Funds	$ 32,696	$ 31,456	$ 32,383	$ 34,054
Other Categorical Grants	807	830	840	839
Inter-Fund Revenues	348	335	331	331
Total City & Inter-Fund Revenues	$ 33,851	$ 32,621	$ 33,554	$ 35,224
Federal Categorical Grants	4,733	4,646	4,635	4,625
State Categorical Grants	8,626	8,560	8,635	8,706
Total Revenues	$ 47,210	$ 45,827	$ 46,824	$ 48,555
EXPENDITURES				
Personal Service				
Salaries and Wages	$ 17,062	$ 17,264	$ 17,253	$ 17,153
Pensions	3,376	4,107	4,515	4,502
Fringe Benefits	5,152	5,431	5,722	6,068
Subtotal – Personal Service	$ 25,590	$ 26,802	$ 27,490	$ 27,723
Other Than Personal Service				
Medical Assistance	$ 4,766	$ 4,997	$ 5,194	$ 5,401
Public Assistance	2,293	2,302	2,303	2,303
Pay-As-You-Go Capital	200	200	200	200
All Other	13,168	12,784	12,962	13,140
Subtotal – Other Than Personal Service	$ 20,427	$ 20,283	$ 20,659	$ 21,044
Debt Service	3,339	3,467	4,027	4,299
Budget Stabilization and Prepayments[1]	(1,300)	(220)	- - -	- - -
General Reserve	300	300	300	300
Subtotal – Expenditures	$ 48,356	$ 50,632	$ 52,476	$ 53,366
Less: Intra-City Expenses	(1,146)	(1,131)	(1,130)	(1,130)
Total Expenditures	$ 47,210	$ 49,501	$ 51,346	$ 52,236
Gaps To Be Closed	**$ - - -**	**$ (3,674)**	**$ (4,522)**	**$ (3,681)**

Source: NYC Office of Management and Budget

[1] Budget stabilization and prepayments in FY 2004 total $1.9 billion, including prepayments of subsidies of $480 million, lease debt service of $71 million, and budget stabilization of $969 million. In addition, a TFA grant in FY 2004 increased FY 2005 tax revenue by $400 million, bringing the total FY 2004 prepayment benefit in FY 2005 to $1.9 billion. In FY 2005, $220 million is set aside to prepay FY 2006 debt service.

Table 2
OSDC Risk Assessment of NYC Financial Plan
(in millions)

	Better/(Worse)			
	FY 2005	**FY 2006**	**FY 2007**	**FY 2008**
Gaps per June 2004 Plan	**$ - - -**	**$ (3,674)**	**$ (4,522)**	**$ (3,681)**
Anticipated State Aid[2]	(400)	(400)	(400)	(400)
TSASC Trapping Event	(116)	(59)	(61)	(60)
Productivity Savings	(95)	(290)	(300)	(300)
Education Funding[3]	(83)	(265)	(493)	(791)
Uniformed Agency Overtime	(75)	(75)	(75)	(75)
Anticipated Federal Aid	(50)	- - -	- - -	- - -
Teacher Sabbaticals[4]	(34)	(34)	(34)	(34)
Tax Revenue	200	- - -	- - -	- - -
Pension Fund Contributions	30	75	135	210
OSDC Risk Assessment	**(623)**	**(1,048)**	**(1,228)**	**(1,450)**
Gaps to be Closed	**$ (623)**	**$ (4,722)**	**$ (5,750)**	**$ (5,131)**
Other Risks and Potential Offsets				
General Reserve[5]	300	300	300	300
Tax Reduction Program	300	305	310	64
Savings from Prior Years' Expenses	250	- - -	- - -	- - -
Pay-As-You-Go Capital	200	200	200	200
Wage Increases at the Projected Inflation Rate[6]	- - -	(220)	(700)	(1,200)

[2] The State has extended for four months the temporary repeal of the sales tax exemption on clothing and footwear items that cost less than $110. Since the June Plan includes $46 million based on an assumption of a two-month extension, the actual amount will be somewhat greater.

[3] The Governor, the Speaker of the State Assembly, and the Senate Majority Leader have all made proposals to change the State education aid distribution formula to comply with the Court of Appeals ruling that the current distribution shortchanges New York City. All three proposals also would require the City to increase its contribution, and the estimates shown represent the amount of funding the City might need to allocate to education, beyond the amounts already allocated in the June Plan for operations, in order to comply with the Governor's proposal.

[4] Since the City has met the State maintenance of effort requirement for FY 2005 and does not intend to fund these costs, the Department of Education will have to identify resources from alternative actions.

[5] The City also set aside $220 million in a budget stabilization fund to narrow the FY 2006 budget gap. While these resources could be drawn upon, if necessary, to help maintain FY 2005 budget balance, the FY 2006 budget gap would widen to the extent that these resources are used in FY 2005.

[6] Wage increases at the projected rate of inflation, without offsetting productivity savings for fiscal years 2006 through 2008, would increase the projected gaps by the amounts shown in the table.

II. Economic Overview

The economic outlook has improved as job gains have finally begun to accelerate along with the rest of economy. With business confidence and spending on the rise, the national economy created nearly 1 million jobs from March to June of this year, a pace not seen since early 2000. This growth, coupled with wage gains, will help sustain the economic expansion. However, with the gross domestic product (GDP) growing at an average annual rate of 5.4 percent during the last three quarters, and oil prices temporarily rising to $40 per barrel, inflation has again become a concern. With higher demand than supply, businesses have regained some pricing power as they begin to pass on cost increases to their customers. In response to growing inflationary concerns, the Federal Reserve raised interest rates by 25 basis points at its June 2004 meeting. This long-expected move marks the beginning of a gradual tightening of monetary policy after more than three years of record-low interest rates.

The City projects that the national economy will grow 4.8 percent in calendar year 2004 (the fastest annual rate of growth in about 20 years), driven largely by double-digit growth in business spending. GDP growth is then expected to slow to around 3.7 percent annually in the 2005 through 2007 period before falling to 2.6 percent in 2008, when both consumer and business spending could slow in response to gradually rising interest rates. National employment is expected to grow by 1.1 percent in 2004, with the rate of gain peaking at 2.3 percent in 2005. The unemployment rate is projected to drop to 5.3 percent over the same two-year period. Employment growth is then expected to slow to 1 percent by 2008, and the unemployment rate is projected to stabilize at the 2005 level.

The City's economy has begun to recover after a three-year contraction that was longer and deeper than the nation's. Job growth has resumed; the local economy created 7,100 private sector jobs in the first five months of 2004 compared to the same period one year earlier. Employment gains in the educational and health services sector have been joined by growth in the sectors of leisure and hospitality, professional and business services, and information. Other sectors—financial activities, construction, and manufacturing—continue to struggle, but the City expects that all sectors except manufacturing will show gains in the coming years. According to the City, private sector employment is projected to rise by 1.2 percent in 2004 and 1.6 percent in 2005. The pace of job growth is then projected to decelerate slightly in subsequent years in response to a slowdown in the national economy. As with national employment, the projected pace of job growth in the City is much lower than the pace experienced in the late 1990s.

Increasing profits on Wall Street are also helping the City's recovery. Wall Street firms account for about one fifth of total wages paid to the City, and each new job creates two additional jobs in other industries. Wall Street profits rebounded to $16.8 billion in calendar year 2003, from $6.9 billion in 2002, as the stock markets surged and securities firms trimmed employees to control expenses. Although market gains have been lower so far in 2004, profits at Wall Street firms totaled $5.1 billion in the first quarter of the year, a gain of almost 45 percent compared to the first quarter of 2003. Nonetheless, as the pace of stock market growth cools down and the securities industry resumes hiring, the City projects that Wall Street profits will ease slightly, to $16.4 billion in 2004 and $14 billion in 2005, but then gradually return to the 2004 level by 2008.

The City's economic forecasts remain unchanged from those made in April. At that time, the City's forecasts were mostly consistent with the forecasts from Global Insight and the Blue Chip Economic Consensus, although the City's forecasts of national employment and personal income growth were generally higher than those of Global Insight. Since then, economic data releases have revealed faster employment growth and higher inflation than previously anticipated. The June forecasts from Global Insight are therefore projecting higher employment growth and inflation at the national level in 2004, while forecasts for 2006 through 2008 have been lowered. Global Insight has not yet updated its forecasts for the local economy. City inflation has risen by 3.2 percent in the first five months of this year, compared to the City's forecast of 2.7 percent for all of 2004. The City projects that inflation will slow to an average 2.4 percent annually during the 2005 through 2008 period, with oil prices coming down from current high levels and interest rate increases by the Federal Reserve restraining inflation.

With price stability now threatened by inflation rather than deflation, monetary policy has shifted. Beginning with the June 2004 increase, the Federal Reserve has indicated its intention to raise short-term interest rates in a "measured" way, assuming inflation does not suddenly worsen. Global Insight now projects that interest rates will be raised by 100 basis points to 2 percent by the end of this year, and then to 3.5 percent by the end of 2005. The 2004 forecast is twice what the City and Global Insight forecast a few months ago, and highlights how the Federal Reserve may move faster than initially expected in order to keep inflation in check and the economy from overheating. Thus, we remain concerned that rising interest rates and large federal deficits will put a damper on economic activity.

III. Fiscal Year 2004

The June Plan assumes that FY 2004 will end with a surplus of $1.9 billion, even though spending will exceed the City's initial estimates, because revenues are expected to be higher by $2.4 billion (see Table 3). The higher revenue estimate reflects increased Wall Street activity and real estate–related transactions. The City plans to use $1.7 billion of the surplus to help balance the FY 2005 budget, and will use the remaining $220 million to help narrow the budget gap projected for FY 2006. Although revenues are now projected to be higher by $1.6 billion in FY 2005, this benefit is expected to be offset by higher-than-planned spending. Revenues are projected to be about $900 million higher than previously estimated in each of fiscal years 2006 and 2007, but spending is projected to grow even faster during these years. Consequently, the out-year gaps have grown by $940 million in FY 2006 and by $1.3 billion in FY 2007 since June 2003.

A. Revenue Changes

A surge in revenue collections—primarily tax revenues—is responsible for improvement of the City's fiscal condition in FY 2004. Overall, revenues are expected to be $2.4 billion higher than originally forecast last June, with taxes accounting for $1.9 billion of the increase.

Although an improvement in the economy was factored into the City's original forecasts, the improvement has been much greater than expected. Wall Street profitability has increased markedly, with profits in calendar year 2003 reaching $16.8 billion—the second-highest level on record—compared to $6.9 billion in 2002. The higher profits translated into higher income, which has flowed through the City's economy. A recent report from this office highlighted the link between Wall Street and job creation and income flows.[7]

Business tax collections rose by 21 percent through May 2004 compared to the same 11-month period in the last fiscal year, and the City has raised its forecast for these taxes by $453 million since June 2003. Personal income tax collections have increased by nearly 25 percent during this 11-month period (although part of that growth is due to the tax surcharge on upper-income residents), and the personal income tax forecast has been raised by $313 million since June 2003. Finally, record-low interest rates have continued to encourage residential and commercial real estate sales and mortgage refinancings. Collections for the mortgage-recording and real

[7] See OSDC's recent report 1-2005, *The Impact of Wall Street on Jobs and Tax Revenues*, April 2004.

property transfer taxes have risen 37 percent in the first 11 months of the fiscal year, and the forecast for these taxes is now $859 million greater than it was in June 2003.

Table 3
Financial Plan Reconciliation
Cumulative Changes Since the June 2003 Plan
(in millions)

	Better/(Worse)			
	FY 2004	**FY 2005**	**FY 2006**	**FY 2007**
Surplus/(Gaps) per June 2003 Plan	**$ - - -**	**$ (2,014)**	**$ (3,238)**	**$ (3,285)**
Revenues				
Tax Revenues	1,933	1,008	801	783
MBBA Proceeds for Education[8]	197	- - -	- - -	- - -
Reimbursement for Stock Exchange Costs	71	- - -	- - -	- - -
Delay in Airport Lease Payment	(200)	200	- - -	- - -
Other Non-Tax Revenue	404	412	134	137
Subtotal	**2,405**	**1,620**	**935**	**920**
Expenditures				
Medicaid	(448)	(388)	(475)	(668)
Collective Bargaining	(333)	(652)	(580)	(574)
Uniformed Agency Overtime	(164)	(98)	(98)	(98)
Private Bus Subsidy	(75)	(159)	(157)	(161)
Public Assistance	(59)	(69)	(69)	(69)
Health and Hospitals Corporation	- - -	(200)	(150)	(150)
Pension Contributions	195	133	143	136
Debt Service	278	264	127	(52)
City Council Initiatives[9]	- - -	(280)	- - -	- - -
Other Agency Expenses	(149)	(710)	(616)	(603)
Subtotal	**(755)**	**(2,159)**	**(1,875)**	**(2,239)**
Other Changes				
Agency Actions[10]	312	- - -	- - -	- - -
Reestimate of Prior Years' Expenses	300	- - -	- - -	- - -
General Reserve	260	- - -	- - -	- - -
Pay Down Debt[11]	(100)	- - -	- - -	- - -
MAC Refinancing Initiative	(502)	502	- - -	- - -
Net Change During FY 2004	**1,920**	**(37)**	**(940)**	**(1,319)**
Surplus/(Gaps) per June Plan	**$ 1,920**	**$ (2,051)**	**$ (4,178)**	**$ (4,604)**

Sources: NYC Office of Management and Budget; OSDC analysis

[8] The Municipal Bond Bank Agency (MBBA) issued bonds to cover State obligations for prior years' education aid.

[9] The budgetary impact was partly offset by $65 million in cost-reduction initiatives.

[10] The recurring values of these actions have been reflected in the FY 2005 gap-closing program.

[11] The City increased the amount set aside for pay-as-you-go capital financing by $100 million, to a total of $200 million, during FY 2004 and later redirected those resources to pay down high-coupon debt due in FY 2006.

In addition, the City received $424 million in bond proceeds from the Municipal Bond Bank Agency in FY 2004, which were not anticipated in the 2003 June Plan. The proceeds represent a lump sum payment in lieu of State education aid that was owed to the City from prior school years. About half of the amount was used to remove a receivable from the City's books, and the remaining $197 million was used to fund the City's operating budget. The State provided the City with $62 million for prior-year payments in the current fiscal year, and the City assumes that the State will appropriate a similar amount to pay debt service on the bonds over the next 20 years. In another transaction, the Industrial Development Agency issued bonds to reimburse the City for $71 million in costs associated with the initial development of the proposed expansion site of the New York Stock Exchange—a project that was cancelled in the wake of the World Trade Center attack. The City also received $151 million from the Federal Emergency Management Agency to cover previously incurred expenses, such as enhanced security and disability pension costs, related to the attack on the World Trade Center.

B. Expenditure Changes

Compared with the estimates in the 2003 June Plan, the 2004 June Plan assumes that agency and programmatic spending will be higher by a net total of $755 million in FY 2004, about $2.2 billion in FY 2005, $1.9 billion in FY 2006, and $2.2 billion in FY 2007.

The rapid and unexpected growth in Medicaid and the expected cost of new collective bargaining agreements account for the entire net increase in spending during FY 2004, and for more than half of the increase in subsequent years. Medicaid spending is expected to be 11 percent higher than projected one year ago because enrollment in the Family Health Plus program has grown much faster than expected. The 2004 June Plan now assumes that Medicaid will cost $448 million more in FY 2004 than projected last June, and $668 million more by FY 2007. In addition, the June Plan assumes that all of the municipal unions will reach new labor agreements that have economic terms similar to the agreement negotiated with District Council 37. That agreement provides for a cash payment of $1,000 per employee upon ratification; a 3 percent wage increase retroactive to July 1, 2003; and a 2 percent wage increase at the beginning of FY 2005 that will be funded with savings from productivity and other operational savings.

In addition, overtime costs in the uniformed agencies are projected to be higher by $164 million in FY 2004, and public assistance costs have increased because of rising caseloads and a State increase in benefit levels. All other agency costs are projected to exceed the estimates made last June, by $149 million in FY 2004 and by

$603 million by FY 2007, reflecting the costs of implementing the new lead abatement law; creating a third-grade intervention program at the Department of Education; resuming weekly recycling and more frequent garbage pickups; developing a new integrated 911 system; maintaining funding for parks and zoos; and providing health and welfare services. The City Council also added a net of $215 million to the budget during the adoption process to fund various programs, such as libraries, child care, and after-school care.

Contrary to what was assumed in the January Plan, the MTA has not assumed the operational or the financial responsibility of the private bus companies. Instead, the City has agreed to continue to directly subsidize the private bus lines until December 4, 2004, when the MTA will take over operational responsibility. The MTA has promoted legislation that would create a new regional bus company that would include the private bus lines. The Transport Workers Union, which represents most transit employees, has expressed concerns about the takeover, particularly as it relates to service levels, employee benefits, and civil service protections.

The growth in City-funded spending will be partly offset by a reduction in pension contributions and debt service costs. Pension contributions are now projected to be $195 million lower in FY 2004 than projected in June 2003 because of actuarial reestimates, returns that were slightly higher than expected in FY 2003, and lower financial services fees. Similarly, debt service costs are projected to be lower than projected in the 2003 June Plan, by $278 million in FY 2004, because interest rates and seasonal borrowing needs were lower than anticipated and because the FY 2003 surplus was $110 million greater than assumed in the 2003 June Plan.

C. Other Changes

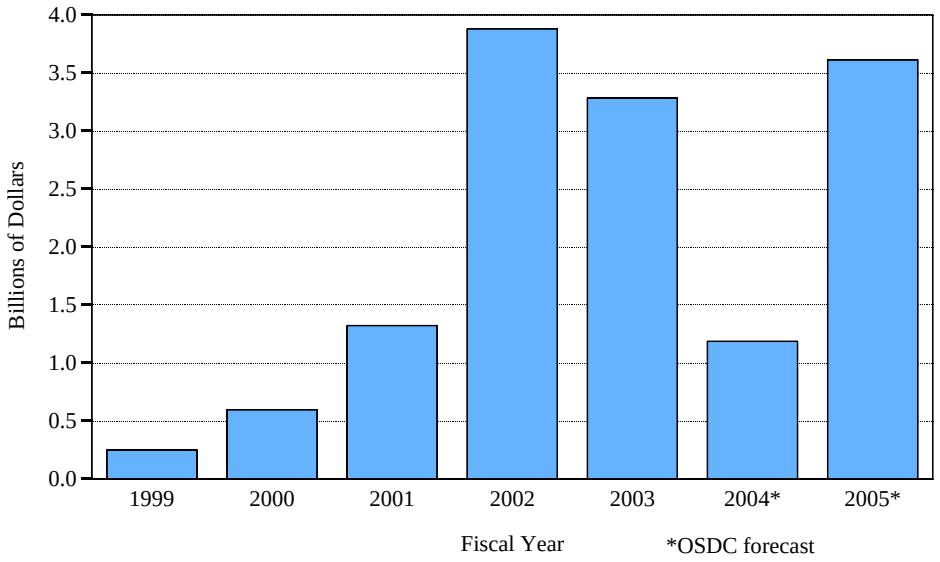
The City made other, mostly technical changes in its four-year financial plan over the past year. As usual, the City drew down the current-year general reserve by $260 million as the year progressed, leaving a balance of $40 million; and recognized savings of $300 million from overestimating prior years' expenses. In addition, during FY 2004 the City increased the amount set aside for pay-as-you-go capital financing by $100 million, to a total of $200 million, but later redirected these resources to pay down high-coupon debt due in FY 2006. The City should be commended for this action, which not only narrowed the FY 2006 budget gap by $196 million but also saved $12 million in FY 2005.

IV. Balancing the FY 2005 Budget

The June Plan includes $3.6 billion in nonrecurring resources (see Appendix A) to help balance the FY 2005 budget—three times more than the $1.2 billion that benefited the FY 2004 budget (see Graph 1). Previously, the City had reduced its reliance on one-time resources as the 1990s progressed and the local economy boomed, but during fiscal years 2002 and 2003 the City resorted to unprecedented levels of nonrecurring resources, including deficit financing, in the wake of the recession and the attack on the World Trade Center. In FY 2004, the City was able to reduce its reliance on nonrecurring resources because the economy improved faster than expected and revenues exceeded the City's initial estimate for FY 2004 by $2.4 billion.

Graph 1

Nonrecurring Resources



Sources: NYC Office of Management and Budget; OSDC analysis

After the use of nonrecurring resources, excluding the $1.7 billion portion of the FY 2004 surplus that was allocated to FY 2005, the FY 2005 budget gap was about $2.1 billion. The June Plan assumes that the surplus transfer from FY 2004 and a combination of City, State, and federal actions will close this gap, fund a modest tax reduction program, and pay a small portion of the City's capital program on a pay-as-you-go basis (see Table 4). Because the City is relying on nonrecurring actions to

balance the FY 2005 budget, however, the City is projecting large budget gaps of $3.7 billion for FY 2006 and $4.5 billion for FY 2007.

Table 4
FY 2005 Gap-Closing Program
(in millions)

	Better/(Worse)		
	FY 2005	**FY 2006**	**FY 2007**
Gap to be Closed	**$ (2,051)**	**$ (4,178)**	**$ (4,604)**
FY 2004 Surplus Transfer	1,700	220	- - -
Agency Actions	389	193	192
State Actions	400	400	400
Federal Actions	50	- - -	- - -
Pay Down FY 2006 Debt	12	196	- - -
Tax Reduction Program	(300)	(305)	(310)
Pay-As-You-Go Capital	(200)	(200)	(200)
Total	**2,051**	**504**	**82**
Remaining Gaps	**$ - - -**	**$ (3,674)**	**$ (4,522)**

Sources: NYC Office of Management and Budget; OSDC analysis

A. Agency Actions

The June Plan includes a modest agency program comprised of revenue enhancements and expense reductions that are valued at $389 million in FY 2005 and less than $200 million in subsequent years. About two thirds of the $362 million in expense reductions in FY 2005 would come from spending reestimates and from actions that would shift costs to other levels of government. The balance would come mostly from reducing civilian staffing levels at the Police and Correction departments; overtime reductions, which we do not believe are achievable; and savings in the Department of Education. The Department had planned to save $34 million annually by reducing the number of teacher sabbaticals, but the union representing the teachers won a grievance against this proposal and thus alternative actions will have to be taken to generate these savings.

B. State Actions

The June Plan assumes that New York State will provide the City with an additional $400 million in annual gap-closing assistance, but a new State budget is now more than three months overdue. In January 2004, the Mayor presented the State with a menu of actions to choose from that, in total, would benefit the City's budget by $1.1 billion. The largest of these items included a State takeover of the local share of Family Health Plus ($342 million), Medicaid cost-containment ($200 million),

removal of the State caps on reimbursement for social service administrative costs ($152 million), and a State takeover of the local share of Medicaid long-term care costs ($117 million).

In the aggregate, the Governor's proposed executive budget for State fiscal year 2004-2005 would provide the City with $362 million in budget relief (see Table 5)—slightly less than anticipated in the Mayor's budget for City fiscal year 2005—and another $56 million in additional education aid (for a further discussion, see "Semi-Autonomous Agencies," page 37). As of July 14, 2004, however, budget negotiations between the Governor and the Legislature were stalled, and the amount and form of any additional assistance to the City remains uncertain. For a detailed discussion of the Governor's proposals see OSDC report 13-2004, *Review of the Five-Year Financial Plan for the City of New York*, issued February 12, 2004.

Table 5
Impact of the Governor's Proposed Budget on FY 2005
(in millions)

	Better/(Worse)
Sales Tax Exemption	$ 152
Medicaid Cost-Containment	141
State Takeover of Medicaid Long-Term Care Costs	33
Early Intervention Cost-Containment	34
Child Welfare and Public Assistance	(49)
Other	51
Subtotal Gap-Closing Aid	**362**
Education Aid[12]	56
Total	**$ 418**

Sources: NYS Division of the Budget; OSDC analysis

The Governor's proposed budget also recommended the repeal of the sales tax exemption on clothing and footwear items that cost less than $110. The exemption, which originally became effective on March 1, 2000, was temporarily repealed for a one-year period beginning on June 1, 2003, to help both the State and City close large budget gaps. In its place, the Governor has proposed four one-week tax holidays for purchases under $500. Since the April Plan assumed that the original exemption

[12] The Governor also proposes the elimination of $62 million in education aid that was intended to pay off claims for prior years' State education aid or to fund debt service on bonds that were issued by the Municipal Bond Bank to reimburse the City for past education aid claims. Because there is no debt service on these bonds until FY 2006 and there are no outstanding claims, the Governor maintains that this cut would have no adverse impact. The City maintains that this represents a cut because the City was permitted by the State to use these resources during fiscal years 2003 and 2004 to fund ongoing educational services.

would be reinstated, its repeal would increase revenues by a net of $152 million in FY 2005. The State has postponed the restoration of the exemption for four months, which will benefit the City's budget by at least $46 million, pending the outcome of State budget negotiations.

C. Federal Actions

The June Plan assumes that the federal government will provide the City with $50 million in gap-closing assistance in FY 2005 alone, which is far less than the $300 million annual increase anticipated in the January Plan. While it is still early in the federal budget process, the prospects for any additional federal gap-closing assistance are poor given the size of the projected federal budget deficits. In fact, the President's proposed budget would eliminate funding to the State Criminal Alien Assistance program, which would cost the City up to $15 million in FY 2005; and would not restore Medicaid funding for legal immigrants. In addition, the President has proposed a large reduction in funding for Section 8 housing vouchers, which could result in the loss of 10,872 vouchers in New York City.

As part of the federal assistance package to New York City following the terrorist attack on the World Trade Center, the federal government authorized the City and the State to refinance for a second time up to $9 billion of outstanding tax-exempt bonds. While the State has used most of its share, the City has $1.3 billion remaining and is seeking an extension, from December 2004 to December 2009. The U.S. Senate recently approved a one-year extension, which, if enacted, would reduce debt service costs by an estimated $20 million in FY 2005.

D. Tax Reduction Program

The Mayor and the City Council negotiated a tax reduction program valued at $300 million in FY 2005, $305 million in FY 2006, $310 million in FY 2007, and $64 million by FY 2008. Both elements of the program—a rebate of real property taxes for homeowners and an earned income tax credit—require approval by the State Legislature and the Governor. A bill authorizing both elements was submitted to the Legislature, but was not approved before the Legislature recessed. Although the Governor and the leaders of the Legislature have proclaimed their support for the bill, final action on the bill has been linked to a resolution of the State budget.

1. Real Property Tax Rebate

The proposed real property tax rebates would give up to $400 to qualified residential property owners beginning in FY 2005. Rebates would be offered for three years at an annual cost of $250 million. The State legislation that would authorize the rebate would also require the City to eliminate the rebate before raising property tax rates, to prevent future tax increases during this three-year period from falling disproportionately on commercial property owners.

The proposed rebate would apply only to those owners of one-, two-, and three-family homes, cooperative apartments, and condominiums who paid property taxes in the prior fiscal year and who could prove that the property was their primary residence. The rebate would be a fixed amount equivalent to the average tax increase for class 1 properties (one-, two-, and three-family homes) in FY 2004. Because the rebate would not vary by location, size, or type of home, it would provide a proportionally greater benefit to properties of lower value, which are generally in the outer boroughs. Taxpayers would need to apply for the rebate, although owners would automatically receive a rebate if they are currently enrolled in the New York State School Tax Relief (STAR) program.

2. Earned Income Tax Credit

Beginning with filings for the 2004 tax year, the City plans to offer a new earned income tax credit to offset City personal income taxes, at a cost of $50 million in FY 2005 and slightly higher amounts in subsequent years. Taxpayers would calculate the City's credit as 5 percent of the federal earned income tax credit. The value of the federal credit is adjusted annually for inflation and varies with income level and the number of dependents. For the 2003 tax year the maximum federal credit was $4,204, and the credit was fully phased out for income levels above $34,692. Like the federal credit, the City's credit would be refundable—if the credit exceeded any City personal income tax liability due (after any other available credits had been taken), the amount in excess would be refunded to the taxpayer. Taxpayers would need to file in order to receive the credit, and the credit would be apportioned for taxpayers who changed their City resident status. The credit would be administered in conjunction with the State's earned income credit (which is calculated as 30 percent of the federal credit). About 700,000 City taxpayers claim the State's earned income credit. For each year that the City wanted to offer the credit, the City would need to notify the State by passing a local law by July 31 of that year.

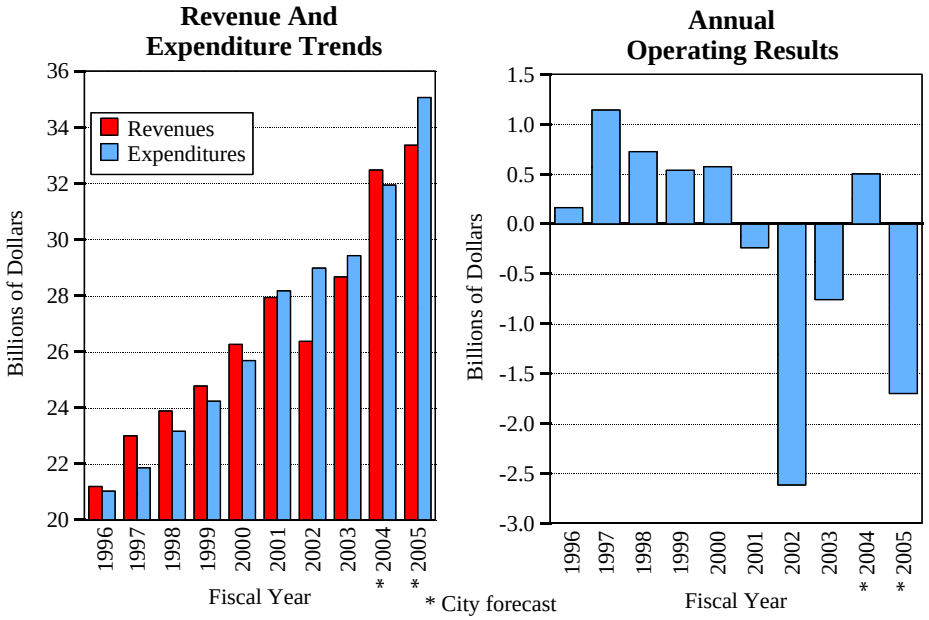
E. Pay-As-You-Go Capital Financing

The June Plan assumes that $200 million in operating budget resources will be devoted to funding the capital program on a pay-as-you go basis during fiscal years 2005 through 2008. The use of operating budget resources eliminates the need to borrow $800 million and will save the City about $90 million in interest payments during the Plan period.

V. Revenue and Expenditure Trends

Between fiscal years 1996 and 2000, City-funded spending grew by 22 percent, an annual average growth rate of 5.1 percent—more than twice the local inflation rate.[13] Under normal circumstances, the City would have been unable to support such a rapid rate of growth, but revenues fueled by the Wall Street boom grew even faster (see Graph 2). While expenditures continued their rapid rate of growth in FY 2001—increasing by 9.7 percent—revenues grew more slowly, by only 6.4 percent. Consequently, expenditures exceeded revenues by more than $200 million in FY 2001—a clear sign of fiscal stress, which was masked by the City's practice of transferring the prior year's surplus to the following year.

Graph 2



* City forecast

Sources: NYC Office of Management and Budget; NYC Comptroller's Office; OSDC analysis

Ignoring this warning, the City called for spending to increase by 5.7 percent in the adopted budget for FY 2002. The budgetary impacts of the economic slowdown and the attack on the World Trade Center, however, resulted in a decline in revenues—the first such reduction since FY 1995 and the largest in more than 20 years. The City balanced the FY 2002 budget, but only after taking into account surplus transfers from prior years and $361 million in bond proceeds from the

[13] City-funded expenditures have been adjusted for the City's practice, which can distort expenditure patterns, of transferring the surplus from one year to the next by prepaying a portion of the following year's expenses.

Transitional Finance Authority. In the absence of these resources, the City would have incurred a deficit of $2.6 billion from current-year operations (see Graph 2).[14]

The City was on course in November 2002 to incur an operating deficit of $3.5 billion in FY 2003 as a result of lower revenue forecasts, rising pension costs, and other factors, but instead ended FY 2003 with a deficit of $759 million. The deficit was reduced when the City enacted a mid-year property tax increase and took other actions to generate recurring benefits. The FY 2003 operating deficit was offset by $1.5 billion in bond proceeds (i.e., deficit financing) from the Transitional Finance Authority to cover revenue losses related to the attack on the World Trade Center.

The City is expected to end FY 2004 with a current-year surplus of $503 million—the first such surplus since FY 2000. The surplus reflects a combination of City, State, and federal actions taken last year to help the City balance its budget, aided by better-than-expected improvement in the local economy. A deficit of $1.7 billion is projected for FY 2005 because the growth in nondiscretionary spending is projected to outpace the growth in recurring revenues. Moreover, the City projects out-year budget gaps of $3.7 billion in FY 2006 and $4.5 billion in FY 2007 because of the absence of $3.6 billion in nonrecurring resources used to help balance the FY 2005 budget, and because of continued growth in nondiscretionary spending.

A. Revenue Forecasts

City fund revenues[15] are projected to increase by 2.8 percent in FY 2005, after an expected gain of 7.6 percent in FY 2004 (see Graph 3). The growth in FY 2004 reflected an expected 17.3 percent gain in tax revenues—the largest component of City fund revenues—due to enacted increases in the real property, personal income, and sales taxes that yielded $2.7 billion. Growth also benefited from higher Wall Street collections and a surge in real estate–related transactions. The increases in the personal income and sales taxes will begin to be scaled back in FY 2005, and the City will rebate a portion of the real property tax increase to homeowners during fiscal years 2005 through 2007. Overall, $2.2 billion of the increase is expected to recur in FY 2005. However, the scale-down of the tax increases, coupled with a sharp drop in real estate–related taxes as transactions fall off, is expected to result in a 1.5 percent decline in tax revenue growth in FY 2005. City fund revenues are still projected to grow in FY 2005 as a result of a significant increase in one-time resources. Three of

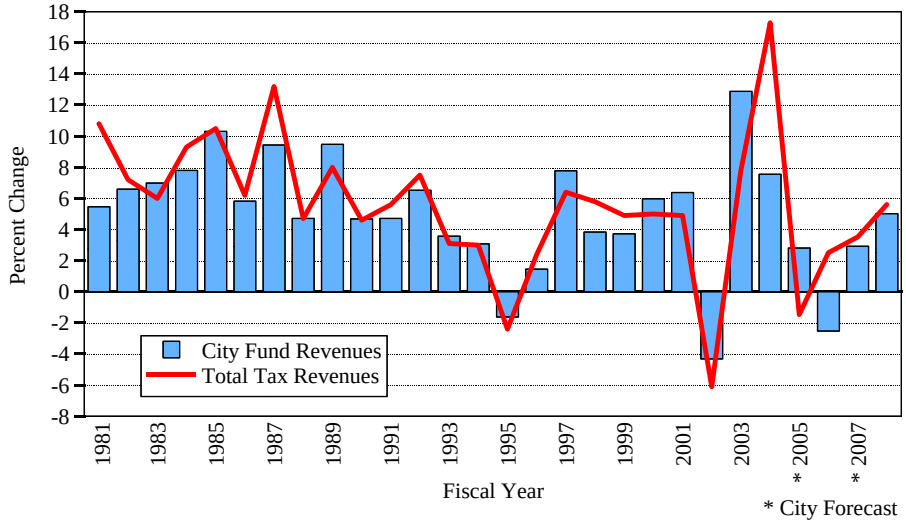
[14] Current-year operations measure revenues and expenditures that were generated in the current fiscal year, and exclude the benefits of prior years' surpluses and deficit financing.

[15] Our estimates of City fund revenues include the portion of personal income tax revenues dedicated to pay debt service on bonds issued by the Transitional Finance Authority, and tobacco settlement revenues dedicated to pay debt service on tobacco bonds.

the largest items—retroactive airport lease payments, the delayed receipt of FY 2004 Municipal Assistance Corporation bond refinancing proceeds, and a land sale to the Battery Park City Authority—yield over $1.3 billion in revenue.

Graph 3

Annual Change in City Fund Revenues and Tax Revenues



Sources: NYC Comptroller's Office; NYC Office of Management and Budget; OSDC analysis

City fund revenues are projected to decrease by 2.5 percent in FY 2006. The loss of the significant one-time resources in FY 2005 pulls down miscellaneous revenue collections by over 30 percent, which more than offsets projected tax revenue gains. Tax revenue growth in FY 2006 is expected to be 2.5 percent, as the continued improvement in the economy overcomes revenue losses from additional phaseouts of the FY 2004 tax increases. However, City fund revenue growth is projected to resume with a gain of 2.9 percent in FY 2007, followed by expected growth of 5 percent in FY 2008. With all the recent personal income and sales tax increases phased out, tax revenues are expected to grow by 3.5 percent in FY 2007, while the end of the property tax rebate lifts growth to 5.6 percent in FY 2008. Miscellaneous revenues show minimal changes between fiscal years 2006 through 2008.

1. Tax Revenues

Real property tax revenues, which comprise 35.6 percent of City fund revenues, are projected to total $11.6 billion in FY 2005, a gain of 1.3 percent over FY 2004 collections. Assessed value growth of 4 percent is partially offset by the

introduction of the real property tax rebate for homeowners. Overall assessed values on the final property tax roll for FY 2005 are about 2 percent lower than the values on the tentative roll used to prepare the Executive Budget, with much of the downward revision affecting values for class 4 commercial properties, most notably hotels. This revision also holds the projected average annual rate of assessed value growth over the remainder of the Plan period to 4.5 percent. After raising average Citywide real property tax rates by 18 percent in January 2003, the Adopted Budget assumes that the average rate will remain unchanged during the Plan period. With the tax rate frozen, the lower assessed values, coupled with the tax rebate, hold average annual growth in the property tax to 4.1 percent during the Plan period (see Table 6).

Table 6
City Fund Tax Revenues
(in millions)

	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008	Four-Yr Avg Growth Rate
Property Tax	**$ 11,397**	**$ 11,550**	**$ 12,013**	**$ 12,557**	**$ 13,374**	**4.1%**
Nonproperty Taxes						
Personal Income Tax	5,528	5,521	5,517	5,543	5,923	1.7%
Sales Tax	3,995	4,004	4,049	4,197	4,373	2.3%
Business Taxes	3,210	3,331	3,519	3,687	3,849	4.6%
Real Estate–Related Taxes	2,110	1,452	1,443	1,515	1,578	-7.0%
Other Taxes	1,789	1,764	1,774	1,813	1,858	1.0%
Subtotal	**16,632**	**16,071**	**16,302**	**16,755**	**17,581**	**1.4%**
Total Taxes	**$ 28,029**	**$ 27,621**	**$ 28,316**	**$ 29,312**	**$ 30,955**	**2.5%**

Note: Includes the impact of the tax reduction program. Personal income tax includes portion of such revenues used to pay debt service on bonds issued by the Transitional Finance Authority. Totals may not add due to rounding.
Sources: NYC Office of Management and Budget; OSDC analysis

With the economy strengthening and the enactment of several temporary tax increases, collections for the City's economically sensitive nonproperty taxes have rebounded, with growth projected to reach 19.2 percent in FY 2004. Personal income, sales, and business taxes constitute over three quarters of the City's nonproperty tax base (see Table 6), and have all been affected by these developments. The rebound in Wall Street profits and year-end bonuses has particularly benefited business and personal income taxes, while low interest rates—and the rush to beat the coming increases in interest rates—have fueled a surge in commercial and residential real estate sales and refinance activity that is reflected in a remarkable and unsustainable increase in real estate–related taxes.

Although the City's tax forecasts already consider an improving economy, several factors will work to hold down expected nonproperty tax revenue growth in

fiscal years 2005 through 2007 (see Table 6). The personal income tax shows very little change from the projected collections of $5.5 billion annually during this period. While both employment and wages are projected to grow, the temporary rate increase will begin to phase out until full expiration is reached during FY 2006, offsetting most of the collection gains from the improving economy.[16] The growth in tax collections was also held down by the new earned income tax credit. After adjusting for rate and base changes, underlying personal income tax collections grow by 3.5 percent in FY 2005, but the offsetting tax changes hold collections to an amount that is essentially unchanged from the FY 2004 level.

Similarly, sales tax collections are projected to remain near $4 billion through FY 2006 as temporary tax increases gradually expire.[17] In August 2004, the exemption for sales tax on individual clothing items that cost less than $110 is scheduled to be restored, although the Governor has recommended its repeal in his executive budget proposal. Negotiations over the State budget have delayed the restoration of the clothing exemption by four months, although the June Plan assumed a two-month extension valued at $46 million. In addition, the one-eighth of a percentage increase in the sales tax rate will expire in June 2005.

By contrast, business tax collections are projected to grow throughout the Plan period, advancing by 3.8 percent in FY 2005, 5.7 percent in FY 2006, 4.8 percent in FY 2007, and 4.4 percent in FY 2008. Wall Street profits, a key factor in collections, are expected to total $16.4 billion in calendar year 2004, down only slightly from the $16.8 billion reported in calendar year 2003. A growing national economy is anticipated to provide additional lift in FY 2005 to the City's export-oriented sectors, such as business and professional services. However, a gradual rise in interest rates by the Federal Reserve could slow the national economy in the later years of the Plan period, contributing to a slight slowdown in the rate of projected business tax growth.

Although low interest rates have helped stimulate collections in the City's real estate–transaction taxes (the mortgage-recording and real property transfer taxes)—leading to a surge in receipts, from around $900 million in FY 2002 to an expected $1.6 billion in FY 2004—the interest rate environment has begun to change, with the Federal Reserve beginning to gradually raise interest rates starting in June 2004. Part of the run-up in collections in FY 2004 has reflected a rush to complete transactions before rates rose significantly. The higher rates will likely begin to adversely affect home affordability and reduce opportunities for refinancing, leading to a pullback in

[16] The temporary personal income tax rate increase is valued at $681 million in FY 2004, $538 million in FY 2005, and $308 million in FY 2006.

[17] The temporary sales tax increase is valued at $332 million in FY 2004 and $133 million in FY 2005.

collections for the two transaction taxes. While the City has expected such a scenario to develop for some time, the long period of record-low interest rates has now started to come to an end. Nonetheless, the City apparently has a large backlog of transactions to process, which may help support collections into early FY 2005. The final real estate–related tax is the commercial rent tax, for which collections were expected to rise by 9.6 percent in FY 2004 as the increase in the real estate tax was passed through to commercial tenants. With employment rising and vacancy rates slowly falling, commercial rent tax collections should gradually improve over the Plan period. Nonetheless, the decline in the two transaction taxes results in a projected decline of over 31 percent for the three real estate–related taxes in FY 2005.

The City's revenue forecasts are based upon an economic scenario of recovery and growth, but recent tax collection data indicate much greater revenue strength than anticipated, and that strength is expected to continue in the short term. Given recent collections experience, both business and personal income tax collections may be understated relative to the City's economic assumptions. Although collections for the real estate–transaction taxes are expected to fall sharply as interest rates begin to rise, the recent surge in transactions has created a backlog in processing that might slightly delay the expected falloff in revenue. Overall, FY 2005 revenues may be $200 million higher than the City currently projects.

2. Miscellaneous Revenues

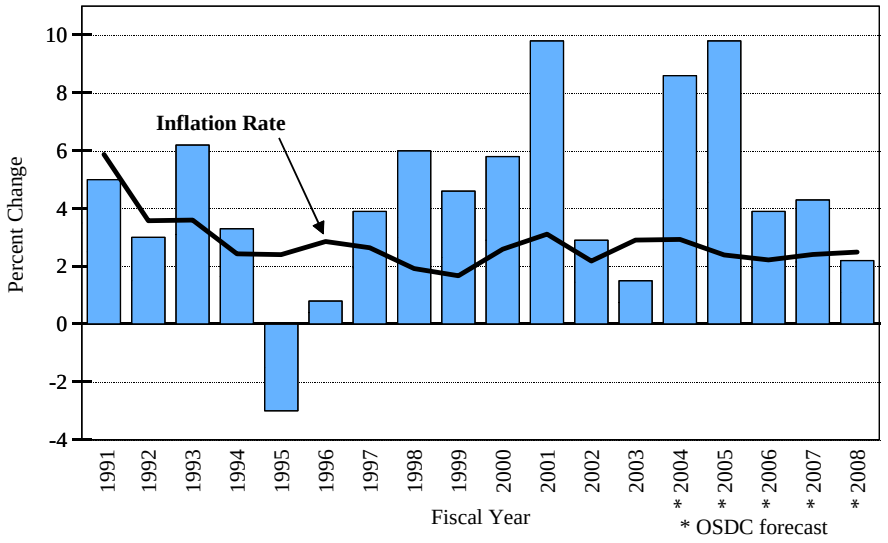
Miscellaneous revenues are non-tax revenues less State and federal grants, and include user fees, rental income, fines, City asset sales, and interest income. These revenues are not economically sensitive, as annual changes are dependent upon discrete actions such as changes in fine or fee levels. Miscellaneous revenues are projected to total $4.5 billion in FY 2005, an increase of $1.3 billion over the amount forecast for FY 2004. These additional revenues primarily reflect the expected receipt of a $783 million lump sum settlement from the Port Authority of New York and New Jersey for a revised lease of the City's two airports, and the reimbursement of $502 million for the debt service incurred by the City associated with the delay in the refunding of MAC bonds. The City also expects one-time revenues of $150 million from a sale of City-owned land to the Battery Park City Authority and a $110 million increase in revenues from the tobacco settlement in FY 2005, although these revenues effectively offset the loss of nonrecurring revenues that had been received in FY 2004. Miscellaneous revenues are projected to decline by $1.5 billion in FY 2006 with the loss of retroactive Port Authority airport lease payments and other nonrecurring resources.

B. Expenditure Forecasts

After increasing far more quickly than the local inflation rate during fiscal years 1997 through 2001, growth in City-funded expenditures during fiscal years 2002 and 2003[18] averaged 2.2 percent, which is slightly lower than the average inflation rate for those years. City-funded spending, however, is projected to resume growth at a rapid rate, and is now projected to surge by 8.6 percent in FY 2004 and 9.8 percent in FY 2005 (see Graph 4), or $5.6 billion during the two-year period. Although expenditure growth is projected to slow to 3.5 percent, on average, during fiscal years 2006 through 2008, this estimate is twice the projected inflation rate and does not take into account the cost of potential wage increases during this period.

Graph 4

Changes in City-Funded Expenditures



Sources: NYC Comptroller's Office; NYC Office of Management and Budget; OSDC analysis

The rapid growth in City-funded expenditures is largely due to nondiscretionary spending. For example, nondiscretionary spending is projected to increase by $4 billion, or 24 percent, between fiscal years 2004 and 2006. Pension contributions alone are projected to rise by 73 percent, or $1.7 billion, and Medicaid is projected to rise by 17 percent over the two-year period.

[18] City-funded expenditures have been adjusted for surplus transfers and include debt service on bonds issued by TSASC and the Transitional Finance Authority.

In FY 2005, pension contributions are projected to rise by $932 million, to $3.2 billion (see Table 7), and then increase by $730 million in FY 2006 and by $407 million in FY 2007. Health insurance costs for municipal employees are projected to increase at an average annual rate of 9.8 percent during the Plan period, while debt service costs[19] are projected to increase by $932 million during the Plan period, an average annual rate of 5.1 percent, and Medicaid costs are projected to increase by $1.1 billion, an average annual growth rate of 6.1 percent (see Table 7). Salary and wage costs are projected to grow by 5.7 percent in fiscal years 2005 and 2006, and then remain level afterwards based on the assumption that a 2 percent wage increase for all City employees planned in FY 2005, as well as all future wage increases, will be funded entirely with productivity savings.

Table 7
City-Funded Expenditures
(Adjusted for Surplus Transfers)
(in millions)

	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008	Four-Year Avg. Growth Rate
Salaries and Wages	$ 9,678	$ 9,956	$ 10,233	$ 10,210	$ 10,095	1.1 %
Debt Service	4,253	4,200	4,318	4,899	5,185	5.1 %
Medicaid	4,140	4,618	4,850	5,047	5,254	6.1 %
Pension Contributions	2,272	3,204	3,934	4,341	4,328	17.5 %
Health Insurance	2,145	2,400	2,622	2,848	3,120	9.8 %
Public Assistance	487	538	542	542	542	2.7 %
Pay-As-You-Go Capital[20]	200	200	200	200	200	0.0 %
Other	8,769	9,945	9,713	9,899	10,106	3.6 %
Total	**$31,944**	**$35,061**	**$36,411**	**$37,986**	**$38,830**	**5.0 %**

Note: Totals may not add due to rounding.
Sources: NYC Office of Management and Budget; OSDC analysis

1. Personal Service Costs

City-funded personal service costs (i.e., salaries, wages, fringe benefits, and pension contributions) are projected to increase by more than $3.6 billion during fiscal years 2005 through 2008. This represents an average annual increase of 5.2 percent and is more than twice the projected inflation rate, even though the June Plan assumes that wage increases granted in FY 2005 and beyond will be funded with

[19] Debt service estimates include City general obligation bonds, revenue bonds of the TFA, MAC, and TSASC, and lease payments. These estimates have also been adjusted in FY 2004 to reflect the prepayment of $624 million in TFA debt service in FY 2003. The July Plan assumes that MAC bonds will be retired, which will generate annual savings of $1 billion in FY 2005 and about $500 million during fiscal years 2006 through 2008.

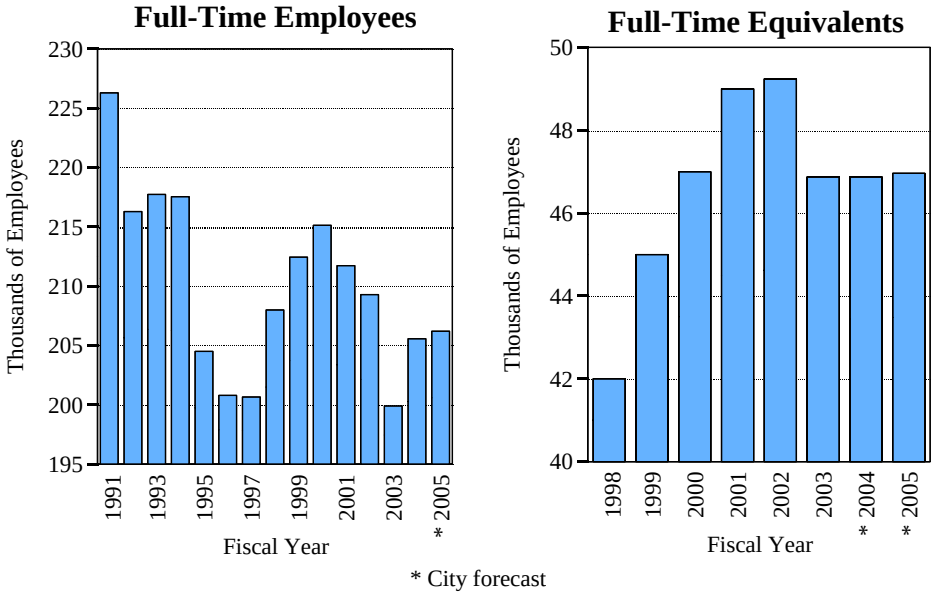
[20] In FY 2004, the City redirected $200 million, which was previously planned for pay-as-you-go-capital financing, to pay down high-coupon debt due in FY 2006.

productivity savings. Instead, the rapid increases in personal service costs reflect the projected growth in health insurance premiums and pension contributions.

The full-time City-funded workforce declined by 15,234 employees during fiscal years 2001 through 2003, but is now projected to rise by 5,668 employees by the end of FY 2004 (see Graph 5). Most of the increase is concentrated in the Department of Education (2,075 employees) and the Department of Social Services (1,113 employees), and includes 293 employees funded under vendor contracts that will be transferred to personal service lines. For FY 2005, the June Plan assumes that the full-time workforce will expand by a net total of 630 employees.

Graph 5

City-Funded Workforce



* City forecast

Sources: NYC Office of Management and Budget; OSDC analysis

The net change includes the transfer of 1,001 employees funded under vendor contracts to personal service lines; the addition of 1,386 employees, including 337 employees at the Department of Housing Preservation and Development for lead abatement activities; and the loss of 1,757 employees through attrition to fund a 2 percent wage increase to members of District Council 37. The number of part-time employees declined by 2,363 employees during FY 2003 but is expected to remain stable during fiscal years 2004 and 2005. (Appendix B shows projected changes in combined full-time and part-time staffing levels.)

Collective Bargaining

On April 20, 2004, the City reached an agreement with District Council 37, which represents most civilian employees. The agreement calls for a one-time cash payment of $1,000 (equal to a wage increase of about 3 percent) payable upon ratification; a 3 percent wage increase retroactive to July 1, 2003; and a 2 percent wage increase in FY 2005 that would be funded entirely with productivity improvements and other operational savings.[21] The District Council 37 agreement would increase wages by 5.1 percent over a three-year period. By comparison, the MTA agreement with the Transport Workers Union increases wages by 6.1 percent over three years, and the State agreement with the Civil Service Employees Association increases wages by 11.0 percent over four years.

To fund the cost of the 2 percent wage increase (estimated to cost $65 million), the agreement calls for a 15 percent reduction in starting salaries for new employees for the first two years of employment, and a reduction in time and leave benefits for new employees. However, the June Plan assumes these savings will be achieved by reducing the civilian workforce by 1,757 employees through attrition. More than half of the positions to be eliminated are located in the City's health and welfare agencies, such as the Department of Social Services, and the Police Department.

The June Plan also assumes that the District Council 37 agreement will set the pattern for contracts with other municipal unions, including those that represent teachers and uniform employees. Consistent with this assumption, the June Plan includes $533 million in FY 2004,[22] $652 million in FY 2005, and about $575 million in subsequent years to fund such agreements. The June Plan, however, does not provide funding for wage increases beyond FY 2005. Wage increases at the projected inflation rates, without offsetting productivity savings, would increase costs by $220 million in FY 2006, $700 million in FY 2007, and $1.2 billion in FY 2008.

Although the City has reached agreement with the unions that represent most civilian employees, applying the productivity terms of the District Council 37 agreement to the unions that represent teachers and uniformed employees could prove challenging. The last agreement with the City's teachers significantly raised starting salaries in recognition of the difficulties of recruiting certified teachers. Similarly, the City has had difficulty recruiting and retaining police officers because of competition from surrounding counties. It is also unrealistic to assume that the City will reduce the

[21] The agreement also provides for an additional wage increase of 1 percent in FY 2005 if the parties can agree on productivity improvements to cover the cost.

[22] The net impact was reduced to $333 million because the City had $200 million in its reserve for collective bargaining.

number of teachers and police officers to fund a wage increase in FY 2005, because the City is under heightened security and the police force has already contracted by 13.7 percent since June 2000. While the City and these unions could negotiate other productivity improvements to offset the cost of a 2 percent wage increase in FY 2005, the failure to do so would increase costs by $95 million in FY 2005, $290 million in FY 2006, and $300 million annually thereafter.[23] The presidents of the United Federation of Teachers (UFT) and the Patrolmen's Benevolent Association (PBA) have already indicated that the District Council 37 agreement is unacceptable.

On May 15, 2004, State Public Employment Relations Board (PERB) declared an impasse in the negotiations between the City and the PBA, which represents 25,000 police officers. PERB has appointed a mediator to help the parties reach a settlement. If mediation is unsuccessful, PERB could appoint a fact-finding panel. Pursuant to law, a fact-finding award is binding for the unions that represent police officers and firefighters. A fact-finding panel set the terms of the last agreement, which, except for contract duration, mirrored the contracts negotiated with most other uniformed employee unions in 2001. The UFT has also requested that PERB declare an impasse in its negotiations. However, PERB is holding its decision in abeyance, pending further efforts to reach an agreement. If PERB were to declare an impasse, it would appoint a mediator and could subsequently appoint a three-member fact-finding panel, which could make nonbinding recommendations to help reach an agreement.

Pension Fund Contributions

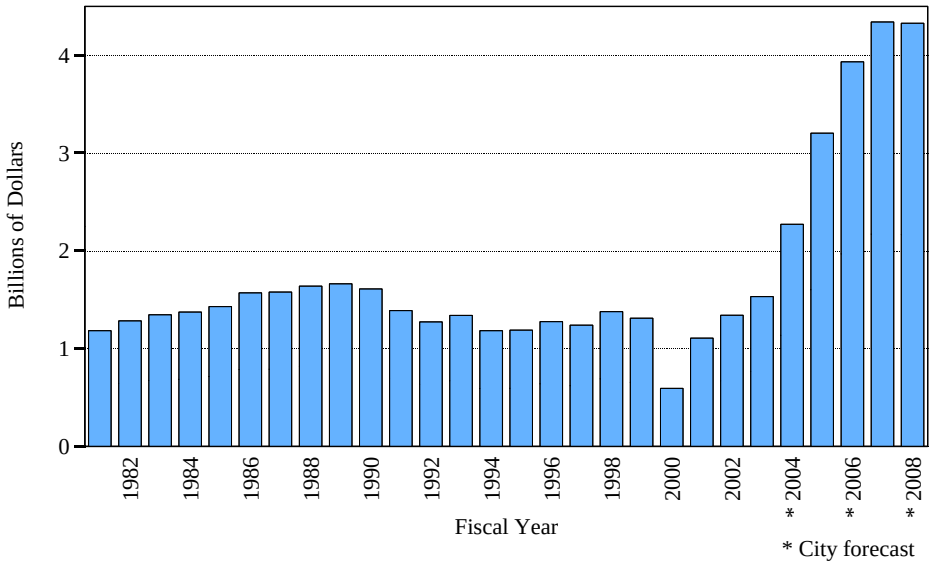
The City's contribution to the pension funds averaged $1.4 billion during fiscal years 1981 through 1999, and totaled $1.5 billion in FY 2003. Contributions are expected to total $2.3 billion in FY 2004, but are projected to rise by $932 million during FY 2005, to $3.2 billion, and to reach $4.3 billion by FY 2007 (see Graph 6). Pension contributions are projected to increase at an average annual rate of 24 percent through FY 2007, which is nearly six times faster than other City-funded expenditures. The rapid rise in pension contributions reflects investment shortfalls during fiscal years 2001 through 2003, which are phased in over a five-year period; and higher benefits and other enhancements that were adopted when the pension funds experienced extraordinary investment gains. Pension contributions are not expected to increase further in FY 2008 because the investment shortfalls will have been fully phased in by that time.

[23] These estimates include teachers and paraprofessionals in the Department of Education, and uniformed employees in the Police, Fire, Correction, and Sanitation departments, where wages follow parity relationships.

The pension funds lost more than 8 percent on their investments in each of fiscal years 2001 and 2002, and gained only 3.8 percent in FY 2003 compared with the actuarial assumption of an 8 percent gain. In FY 2004, the pension funds earned about 16 percent on their investments, twice the assumed rate of return, although most of the gains were achieved during the first half of the fiscal year. As a result of these unexpected gains, the City will be able to reduce its planned pension contributions by $30 million in FY 2005, $75 million in FY 2006, $135 million in FY 2007, and $210 million in FY 2008.

Graph 6

City-Funded Pension Contributions



Sources: NYC Office of Management and Budget; OSDC analysis

An actuarial consultant hired by the City has completed a biennial review of the methodologies and assumptions used to calculate pension contributions, as required by law. The consultant did not propose changes in the investment earnings and wage assumptions, but did propose adjustments in a number of other assumptions, such as overtime, which could increase City pension contributions by approximately $250 million annually. The City's Actuary has not yet made recommendations to the boards of trustees of the funds, but he is considering the consultant's recommendations and other changes, including those that could slow down the projected growth in pension contributions. The changes under discussion include an increase, from five years to seven years, in the phase-in period for gains and losses; a one-year lag in calculating pension contributions; and funding the full cost of cost-of-

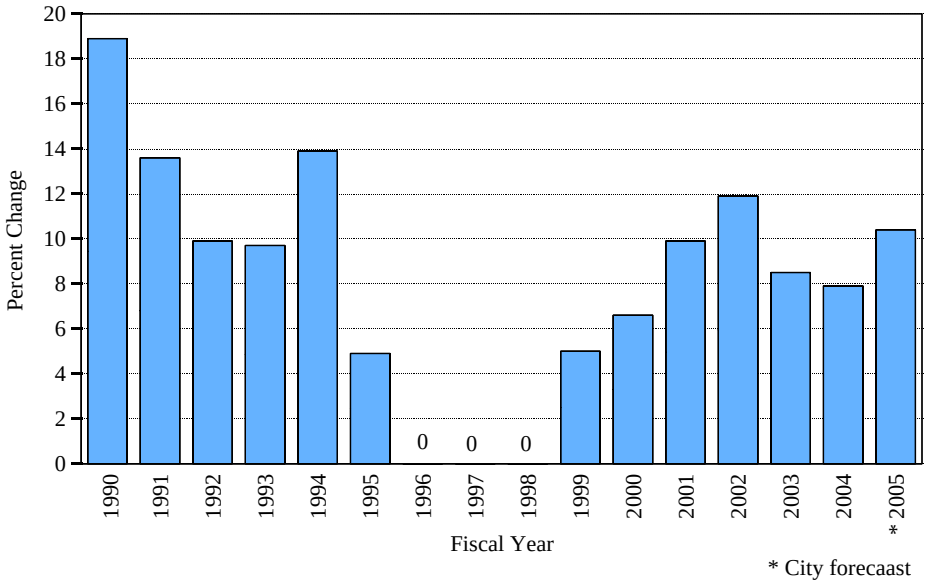
living-adjustments for retirees rather than the current practice of phasing in the costs over a ten-year period.

Health Insurance

City-funded health insurance costs are projected to grow from $2.1 billion in FY 2004 to $2.4 billion in FY 2005 and then to $3.1 billion by FY 2008, reflecting rapidly rising health insurance premiums. Premiums grew at a double-digit pace during the early 1990s, but the City then negotiated a three-year freeze in rates for fiscal years 1996 through 1998 as part of a package to help it balance its budget during a period of fiscal stress. Since then, health insurance premiums have resumed rapid growth, reflecting national cost trends for medical and hospital care (see Graph 7). For example, the Health Insurance Plan of Greater New York (HIP) increased premiums by 9.9 percent in FY 2001, 11.9 percent in FY 2002, 8.5 percent in FY 2003, and 7.9 percent in FY 2004.[24]

Graph 7

Annual Change in Health Insurance Premiums



Sources: NYC Office of Management and Budget; HIP

[24] Under agreements between the City and its unions, premiums paid to HIP determine the City's cost for all municipal insurance providers.

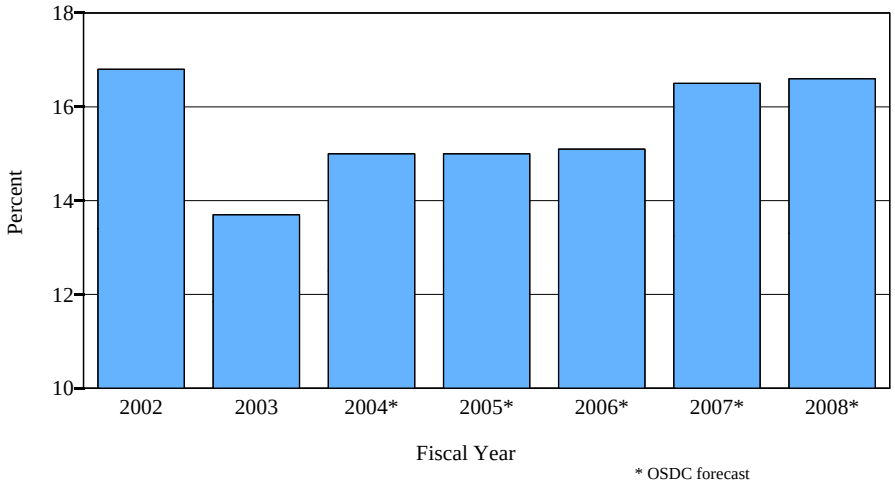
The June Plan reflects HIP's intention to increase premiums for active employees and retirees who are under the age of 65, by 10.4 percent in FY 2005. The Plan assumes that premiums for these employees will increase by 8 percent annually thereafter, which is somewhat lower than increases in the recent past. The June Plan anticipates that health insurance premiums for Medicare-eligible retirees will not increase in FY 2005, but will then increase by 8 percent annually thereafter. Costs were projected to grow even faster but the City reduced its projections to reflect the impact of higher health insurance copayments and deductibles, which will reduce the City's share of these costs and hold down utilization.

2. Debt Service

Debt service costs declined in FY 2003, reflecting savings from bond refundings and the release of reserve funds, but are projected to increase by $943 million in FY 2004 to nearly $4.3 billion, even after adjusting for debt prepayments that can distort expenditure trends. Debt service costs are projected to increase by $932 million by FY 2008, to $5.2 billion, which is an annual average increase of 5.1 percent, or nearly twice the projected inflation rate.

Graph 8

New York City Debt Service Burden



Sources: NYC Office of Management and Budget; OSDC analysis

The debt service burden declined from 16.8 percent in FY 2002 to about 13.7 percent during fiscal year 2003, but is projected to increase to 15 percent in FY 2004 and then steadily rise to about 16.6 percent by FY 2008 (see Graph 8). The

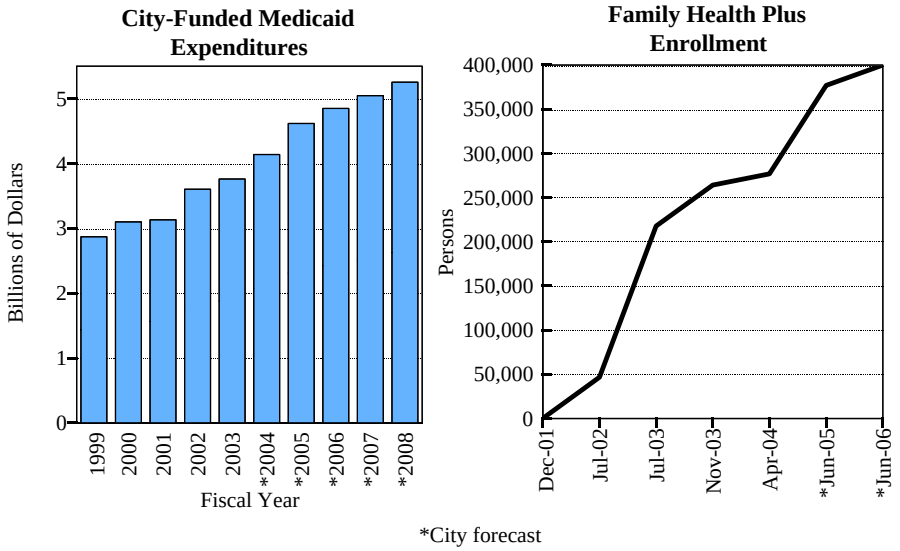
debt service burden[25] was on track to approach 20 percent by FY 2005 but the City refinanced outstanding debt, cut the capital program, and increased property and personal income taxes. In addition, the June Plan anticipates the implementation of the MAC refinancing initiative (see "Municipal Assistance Corporation," page 46), and tax revenues have been growing much faster than previously projected in response to an improving economy.

3. Medical Assistance

The June Plan assumes that City-funded Medicaid expenditures will rise by $480 million, from $4.1 billion in FY 2004 to $4.6 billion in FY 2005, and then increase to $4.8 billion in FY 2006, $5 billion in FY 2007, and $5.3 billion in FY 2008 (see Graph 9). This represents an average annual increase of 6.1 percent during fiscal years 2005 through 2008. Because this rate of growth is faster than the projected growth rate for City fund revenues, Medicaid is projected to consume an increasing share of City fund revenues. Medicaid consumed, on average, 12.5 percent of revenues during fiscal years 1999 through 2003, but would consume 15.1 percent of City fund revenues between fiscal years 2005 and 2008.

Graph 9

Medical Assistance



*City forecast

Sources: NYC Comptroller's Office; NYC Office of Management and Budget; OSDC analysis

[25] The debt service burden is defined as City-funded debt service as a percent of tax revenues and offsetting revenues, including amounts to support TFA and TSASC debt service.

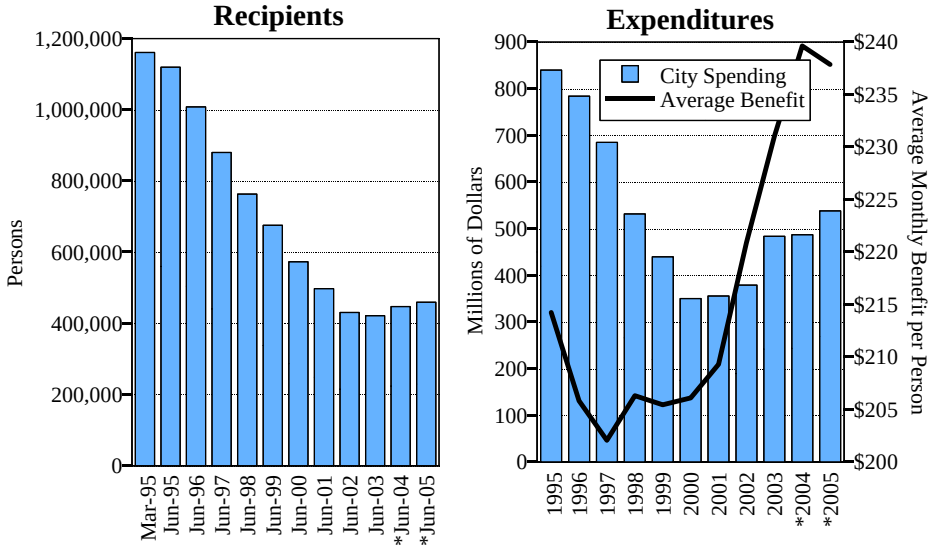
The growth in Medicaid expenditures is attributable to the continuing rise in the cost of medical services for enrollees who are not in Medicaid managed care, the cost of prescription drugs, and the rapid expansion in the Family Health Plus program. Family Health Plus is a managed care program funded by Medicaid that serves adults whose incomes exceed the limits allowed under regular Medicaid. The June Plan projects that enrollment in Family Health Plus will grow by 100,000 to 377,000 in FY 2005, and then stabilize at about 400,000 during FY 2006. The June Plan assumes that the program will cost $342 million in FY 2005, $381 million in FY 2006, and $394 million in FY 2007.

4. Public Assistance

Public assistance in New York State effectively consists of three programs. The largest, Family Assistance, uses the federal welfare block grant to provide aid to families with children for a maximum of five years. The other two programs are components of Safety Net Assistance, which is equally funded by the State and City. One program primarily serves adults and the other serves families who exhaust their federal benefits.

Graph 10

Public Assistance



*City forecast

Sources: NYC Human Resources Administration;
NYC Office of Management and Budget; OSDC analysis

After declining each year since 1995, the public assistance caseload increased through the first five months of FY 2004 by 4 percent, to 439,033 persons. Most of

the increase occurred in the adult Safety Net Assistance program, which added 13,150 recipients. It is expected that the caseload will increase by another 4.5 percent during FY 2005, to 458,902 persons by June 2005 (see Graph 10).

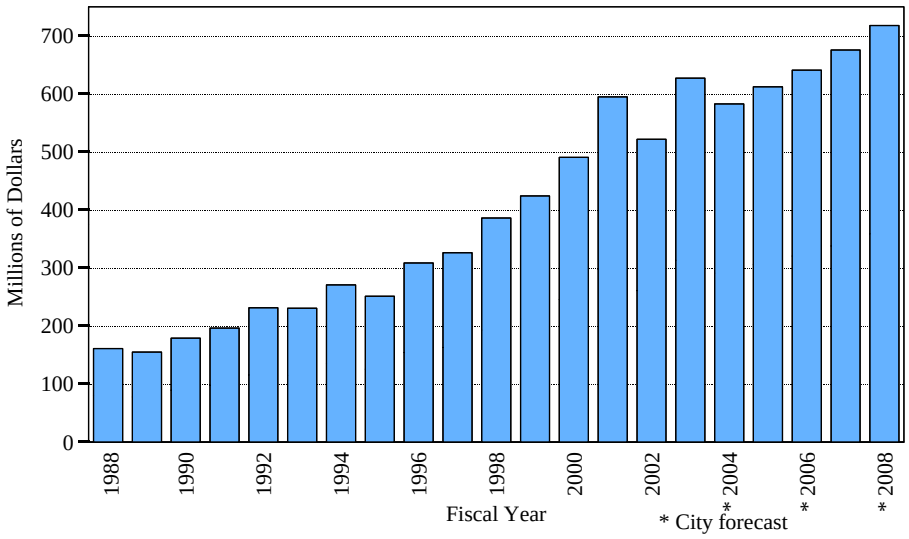
The June Plan assumes that rising caseload and average benefits per person will increase City-funded public assistance spending to $487 million in FY 2004, $538 million in FY 2005, and $542 million annually thereafter. In FY 2001, the average monthly benefit was $209.41, but during 2004 averaged $239.73 per person (see Graph 10). The increase primarily reflects the rising cost of rent in New York City, but also the greater prevalence of cases with more costly needs, such as beneficiaries with chronic illnesses or large families, because most employable recipients have left the caseload.

5. Judgments and Claims

The costs of judgments and claims have increased steadily since FY 1990 and have more than doubled since FY 1996 (see Graph 11). The June Plan assumes that judgments and claims will decline by 7 percent in FY 2004, to $583 million, because the City believes that settlements for cases under a million dollars will be lower, and that settlements of cases over a million dollars will be similar to last year's levels.

Graph 11

Judgments and Claims



Sources: NYC Comptroller's Office; NYC Office of Mangement and Budget

The City's estimates do not reflect any potential liability arising from the Staten Island Ferry accident of October 15, 2003, or from the World Trade Center attack on September 11, 2001. To date, the City has received 190 claims seeking an estimated $3.4 billion for wrongful death, personal injury, and emotional distress related to the Staten Island Ferry accident. In December 2003, the City filed a petition in federal court asking that all claims be consolidated, and that its exposure be limited to $14.4 million (the value of the ferry) under the Federal Maritime Act of 1851.

The World Trade Center disaster generated more than 2,000 lawsuits and notices of claim against the City, with an aggregate value of $13 billion. The City's potential liability has been reduced to $1.6 billion because about 1,900 claimants, mostly firefighters and other emergency response workers, opted to file with the federal Victim Compensation Fund before the deadline of December 22, 2003.

Included in the remaining $1.6 billion in claims is a potential liability of $1.1 billion from the insurers of 7 World Trade Center and from Consolidated Edison and its insurers, alleging that the City was responsible for that building's collapse on September 11, 2001. However, legislation passed by the federal government in the aftermath of the World Trade Center attack limits the City's liability to $350 million: "…all claims, whether for compensatory or punitive damages or for contribution or indemnity arising from the terrorist-related aircraft crashes of September 11, 2001, against the City of New York shall not exceed the greater of the City's insurance coverage or $350,000,000."[26]

The federal government has authorized the creation of an insurance company that would fund $1 billion in potential liability to cover the cost of injuries incurred from debris removal at the World Trade Center site from September 11, 2001, onward, and that would cover current and future health-related claims that may develop against the City and the four contractors it hired for site cleanup. The contractors began work at the site before obtaining insurance from possible lawsuits. The City's Law Department believes that nearly all of the remaining 100 cases, with an aggregate value of about $500 million, will be covered by this insurance.

6. Uniformed Agency Overtime

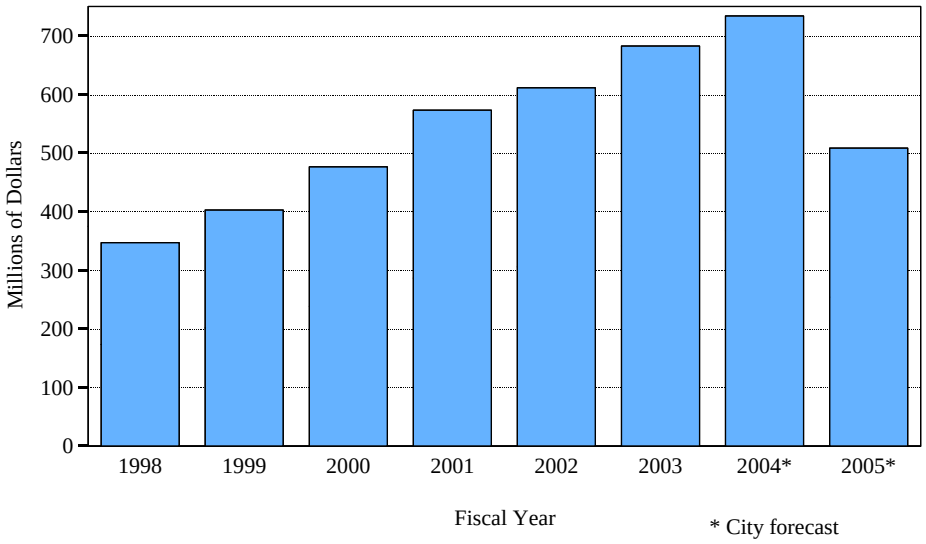
Since FY 1998, overtime costs in the uniformed agencies (excluding overtime associated with the attack on the World Trade Center) have more than doubled, from $347 million in FY 1998 to $734 million planned for FY 2004 (see Graph 12). The rapid and steady rise in costs is largely due to increased security; a reduction in the

[26] *Aviation and Transportation Security Act*, Public Law 107-71, 107th Cong., 1st sess. (November 19, 2001).

size of the police force, which has been partly compensated through overtime; the loss of 343 firefighters during the destruction of the World Trade Center; and the retirement of hundreds of firefighters since the disaster.

Graph 12

Uniformed Agency Overtime



Note: FY 2002 excludes World Trade Center expenses.
Sources: NYC Office of Mangement and Budget; NYC Financial Information Services Agency

The Adopted Budget for FY 2004 assumed that the Police Department would spend $189 million on overtime, but now estimates that police overtime will total $409 million, which would represent a new record (excluding overtime associated with the attack on the World Trade Center). Although the June Plan assumes that overtime will decline to an average of $273 million annually during the Plan period, the City has yet to demonstrate an ability to bring these costs under control. Thus, police overtime costs could exceed the Plan estimates by $75 million annually beginning in FY 2005.

The Fire Department spent a record $178 million on overtime in FY 2003 to maintain adequate staffing with simultaneous high rates of retirement, sick leave, and line-of-duty injuries related to the World Trade Center tragedy. The City now estimates that overtime costs in the Fire Department will total $174 million in FY 2004, but will then decline to $111 million in FY 2005—well below recent trends in actual overtime spending. While this represents an ambitious reduction in overtime costs, our analysis indicates that it may be achievable if the department can maintain its current staffing levels.

VI. Semi-Autonomous Agencies

Covered organizations are semi-autonomous agencies subject to the Financial Emergency Act (FEA) and include but are not limited to the Board of Education,[27] the Health and Hospitals Corporation, the New York City Transit Authority (a component agency of the Metropolitan Transportation Authority), the Off-Track Betting Corporation, and the New York City Housing Authority. The City has a financial relationship with these agencies and may be called upon to provide additional funding to help balance their budgets. In addition, a number of other entities, mostly public authorities, are not subject to the FEA but have a financial relationship with the City. These include the Municipal Assistance Corporation, the Transitional Finance Authority, TSASC Inc., and the New York City Municipal Water Finance Authority. In addition, the City has proposed the creation of a local benefit corporation, the Hudson Yards Infrastructure Corporation, to finance development of the far West Side of Manhattan.

A. Department of Education

In FY 2005, funding for the Department of Education is projected to total $15.1 billion, an increase of $687 million over the FY 2004 level.[28] The City is projected to contribute $5.4 billion for operations and another $2.1 billion for pensions and debt service, which represents 49.5 percent of the Department of Education budget. New York State is projected to contribute $5.9 billion, or 38.8 percent of the department's budget (see Graph 13). The federal government is projected to contribute $1.7 billion, or 11.5 percent of the budget. The balance comes from fees, grants, settlements, and restricted sources.

State law prohibits the City from reducing its funding for education (excluding pension and debt service) from one year to the next, unless there is a reduction in City revenues. The FY 2005 adopted budget includes City funding of $5.4 billion for operations, which exceeds the State's minimum requirement by $218 million, and which would establish a new higher base level for FY 2006.

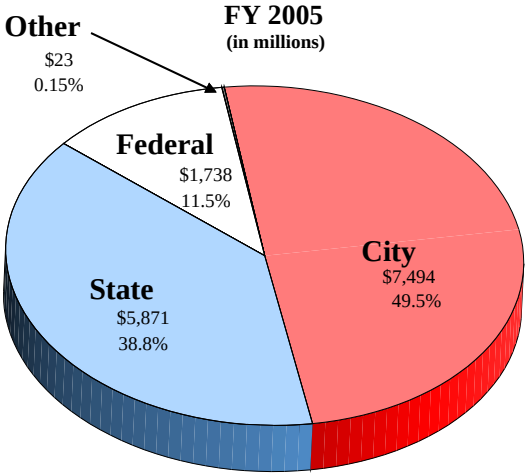
In June 2003, the Court of Appeals ruled that the formula for allocating State education aid was unconstitutional and gave the State until July 30, 2004, to determine the cost of providing a sound, basic education in New York City and to enact necessary reforms. The Governor and the State Legislature, however, have yet

[27] The Board of Education has been renamed the Department of Education by the Mayor, although the legal name remains unchanged.

[28] Estimates adjusted for debt prepayments, which can distort spending patterns.

to agree on a new budget for the fiscal year that began on April 1, and the State Legislature adjourned after approving an emergency appropriations bill to carry the State through August 1, 2004. While the Legislature is expected to reconvene before the July 30 deadline, there is no assurance that it will reach agreement with the Governor on a new funding formula. The Court of Appeals has returned the case to the State Supreme Court, which has begun assembling a panel of special masters to assess the State's compliance with the ruling.

Graph 13
Department of Education
Sources of Funding
FY 2005
(in millions)



Note: Estimates adjusted for debt prepayments.

Source: NYC Office of Management and Budget; OSDC analysis

Although the State has failed to approve a new funding formula, it cannot be due to a lack of suggestions. The Campaign for Fiscal Equity (CFE), plaintiffs in the lawsuit, proposed that spending on operations for education be increased by $8.5 billion over four years, with New York City receiving $5.3 billion of the increase. The CFE also proposed a $9 billion capital plan for New York City and a $1 billion capital plan for other high-need school districts. The New York State Commission on Education Reform, which was appointed by the Governor, recommended that the State increase spending on education by between $2.5 billion and $5.6 billion over five years. A report by Standard and Poor's, which was the basis for the commission's recommendation, suggested that New York City would need between 78 percent and 84 percent of the increase to raise spending to a level comparable to successful school districts in the State.

The Governor recently proposed increasing State education aid to New York City by $2.2 billion over five years; the State Senate majority leader proposed an increase of $1.8 billion; and the Speaker of the State Assembly proposed an increase of $3.9 billion.[29] The Speaker also proposed that the State allocate $1.3 billion to New York City for school construction and renovation. All three proposals would be funded, at least in part, by revenues from an increase in the number of video lottery terminals at race tracks and off-track betting parlors around the State.

Each of these proposals would require that the City of New York allocate additional funds for education over a five-year period. The Senate majority leader proposed that the City increase funding by $554 million; the Speaker suggested an increase of $1.2 billion; and the Governor recommended that the City increase funding by $1.5 billion within five years. While the Governor and the State legislative leaders have yet to reach agreement on a new funding formula, it seems likely that the City will be required to increase its funding. If the Governor's proposal were adopted, we estimate that the City could be required to increase funding beyond the amounts already included in the City's financial plan for operations by $83 million in FY 2005, $265 million in FY 2006, $493 million in FY 2007, and $791 million in FY 2008.

In addition, the Department of Education has proposed a five-year $13.1 billion capital plan for fiscal years 2005 through 2009, which would be funded equally between the State and the City.[30] The department's plan allocates $4.1 billion to bring current facilities to a state of good repair, including the upgrading of lighting, electrical, safety, and security systems; $4.2 billion for system expansion, including the construction and leasing of space to create 90 new schools and 66,000 new seats (5 more schools and 3,000 more seats than the earlier plan); and $4.8 billion for educational enhancements, including $2 billion for restructuring and enhancing the physical facilities of 671 schools where students are not demonstrating math and reading skills at grade level, and $1 billion to upgrade or provide technology to classrooms.

Although the members of the City Council recently approved the department's proposed five-year capital plan, they have expressed several concerns. First, the department does not have a fallback plan if the State does not provide $6.5 billion in capital funding. In addition, the department does not include timelines and cost

[29] The Governor and the State Senate majority leader also proposed increases in federal aid of $1 billion and $515 million, respectively.

[30] While the City's budget includes the City's share, the Governor's proposed budget does not include the State's share of these resources. State legislation, however, has been proposed that would permit the Transitional Finance Authority to issue up to $2.8 billion in bonds to help finance improvements in educational facilities.

estimates for all ongoing projects in its quarterly monitoring report as mandated by the City Council. It is expected that the Department of Education and the City Council will approve a memorandum of understanding that requires the department to obtain the Council's annual approval before proceeding with its capital program.

B. Health and Hospitals Corporation

In January 2004, the Health and Hospitals Corporation ("the Corporation") projected that cash expenses would exceed receipts by $435 million in FY 2005 and by more than $600 million annually in subsequent years. To assist the Corporation in meeting its ongoing cash needs, the April Plan increased the City's support to the Corporation by $200 million in FY 2005 and by $150 million thereafter. Since the underlying causes of the Corporation's budget gaps have not been addressed, the Corporation still projected budget gaps of $273 million in FY 2005 and more than $500 million during fiscal years 2006 through 2008. The June Plan projects operating deficits of $235 million for FY 2005, excluding City prepayments,[31] and more than $500 million for subsequent years.

The major source of the Corporation's budget gaps is inadequate reimbursement for the services it provides to uninsured patients (the Corporation provides care to 460,000 uninsured City residents each year). Also, the cost of providing outpatient services exceeds the Medicaid reimbursement rate (the Corporation provides medical care to 5.6 million outpatient visitors annually). In addition, State Department of Health data indicate that the Corporation has recently lost market share to voluntary and proprietary hospitals for inpatient care, a service for which the Corporation receives full reimbursement of its costs.

To close the projected operating gaps, the Corporation intends to draw down a projected opening cash balance in FY 2005 and to take actions valued at $332 million in FY 2005, $436 million in FY 2006, $511 million in FY 2007, and $536 million in FY 2008 (see Table 8). The largest of these initiatives that require federal or State approval involves resolving old claims for third-party reimbursement, and the Corporation has hired consultants to assist in this effort. An effort to maximize revenue by reducing the number of claims denied by insurers, improving billing processes, and enrolling uninsured patients into public health insurance programs is expected to generate $30 million in FY 2005, $50 million in FY 2006, and $75 million annually thereafter.

[31] In FY 2004 the City prepaid $159 million of its FY 2005 subsidy to the Health and Hospitals Corporation in order to transfer a portion of the City's surplus from FY 2004 to FY 2005. This transaction had the effect of increasing the FY 2005 operating deficit to $394 million because these resources were previously expected in FY 2005. Regardless, the FY 2005 year-end cash balance remains unchanged.

Table 8
Health and Hospitals Corporation
Gap-Closing Program
(in millions)

	FY 2005	FY 2006	FY 2007	FY 2008
State and Federal Actions	$ 212	$ 271	$ 321	$ 346
Spending Reductions	55	80	80	80
Revenue Maximization	30	50	75	75
City Agencies	35	35	35	35
Total	**$ 332**	**$ 436**	**$ 511**	**$ 536**

Sources: NYC Office of Management and Budget; OSDC analysis

C. New York City Transit Authority

The New York City Transit Authority, a covered organization, is the largest component of the Metropolitan Transportation Authority (MTA). On October 28, 2003, the MTA released a revised budget for 2003 and a four-year financial plan for calendar years 2004 through 2007. The 2003 October Plan was the first five-year financial plan released by the MTA since September 1999, and was prepared in accordance with new financial reporting procedures adopted by the agency in response to criticism by the State Comptroller that the MTA's 2002 December Plan secretly shifted surplus resources from 2002 to future years, and did not accurately show the size of the projected budget gaps during the debate over proposed fare and toll increases.

The 2003 October Plan showed budget gaps of $840 million in 2005, $1.3 billion in 2006, and $1.5 billion in 2007, which the MTA attributed to projected increases in debt service and pension costs and the depletion of nonrecurring budgetary actions. Our report on the October Plan[32] commended the MTA for improving its financial plan presentation, but concluded that the MTA had underestimated the size of the gaps by $307 million in 2005, $358 million in 2006, and $649 million in 2007 because the MTA had included speculative resources in the financial plan's baseline estimates.

Specifically, the October Plan underestimated expenditures by $80 million in 2005, $129 million in 2006, and $174 million in 2007 by counting on savings from unspecified cost reductions. In addition, the MTA agencies were directed by MTA headquarters to use employment forecasts prepared by Global Insight, the MTA's

[32] See OSDC Report 10-2004, *Review of the Financial Plan for the Metropolitan Transportation Authority*, issued December 2003.

economic consultant, in making their fare and toll revenue projections—yet MTA headquarters then increased the agency's forecasts by 5 percent in 2005, or $227 million, and by 10 percent in 2007, or $475 million, beyond the increases already assumed by the agencies in their budgets. MTA headquarters based its increases on hoped-for growth in utilization, but offered no economic basis for its projections. We believe it was unreasonable for MTA headquarters to include unsubstantiated increases in utilization in the financial plan, especially ones that contradicted the recommendations of its economic advisor. The MTA financial plan assumes that the MTA board will approve reductions in fare and toll discounts to generate additional revenue if planned increases in utilization do not materialize.

On February 23, 2004, the MTA issued a revised financial plan, which was the first plan to be released under new regulations issued by the State Comptroller. These regulations were designed to further improve the transparency and accountability of the MTA's finances. The February Plan included, as required by the regulations, a certification from the MTA's Executive Director that the financial plan was based on reasonable assumptions and methods of estimations, and that it complied with the Comptroller's regulations; a debt affordability statement; debt service estimates for the next capital program during the financial plan period; and a statement of nonrecurring resources and transactions that would shift resources from one year to another.

The February Plan showed budget gaps of $539 million in 2005, $1.2 billion in 2006, and $1.3 billion in 2007, but still included speculative resources in its baseline estimates even though the Comptroller's regulations define budget gap as "the difference between projected revenues and expenses for any given fiscal year *before* [emphasis added] a proposed fare increase or other proposed management actions that increase revenues or reduce costs." When these speculative resources are excluded, the budget gaps total $846 million in 2005, $1.5 billion in 2006, and $2 billion in 2007. Subsequent to the release of our May 2004 report on the Mayor's Executive Budget, which included a section devoted to the MTA financial plan, the MTA stated its willingness to revise its financial plan presentation in the future (beginning in July 2004) to comply with the Comptroller's regulations.

The MTA also intends to release a preliminary capital program for 2005-2009 in July, and plans to forward a proposed five-year capital program to the Capital Program Review Board for its approval in October. In the absence of an approved capital program for 2005-2009, the February Plan made certain assumptions regarding the size of the next capital program in order to develop debt service projections for calendar years 2005 through 2007. The February Plan assumed that the MTA would use debt to finance about the same portion of the 2005-2009 capital program as it

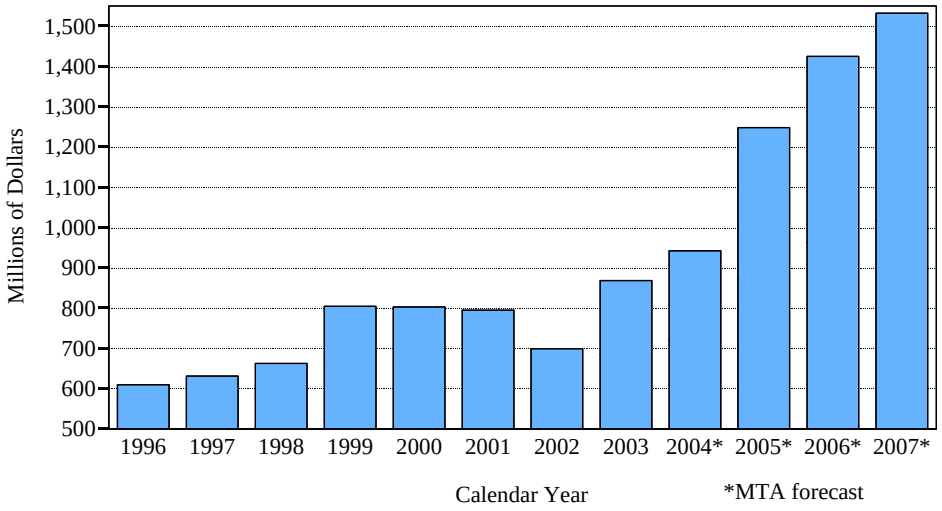
funded during the current capital program. The February Plan anticipated no new resources from the State and only a minimal contribution from the City.

The February Plan assumed that debt service costs used to finance past capital programs and to complete the 2000-2004 capital program would grow from $942 million in 2004 to $1.5 billion by 2007 (see Graph 14). As a result, debt service costs as a percentage of fare and toll revenue would increase from 20 percent in 2004 to 30 percent by 2007. The February Plan further assumed that the MTA would finance $9.8 billion of the next capital program with its own debt, which we estimate would increase debt service costs to $2.3 billion by 2014, placing extraordinary pressure on the operating budget.

Graph 14

MTA Debt Service Costs

(Excluding 2005-2009 Capital Program)



Note: Projections exclude impact of proposed 2005-2009 capital program.

Sources: Metropolitan Transportation Authority; OSDC analysis

D. Off-Track Betting Corporation

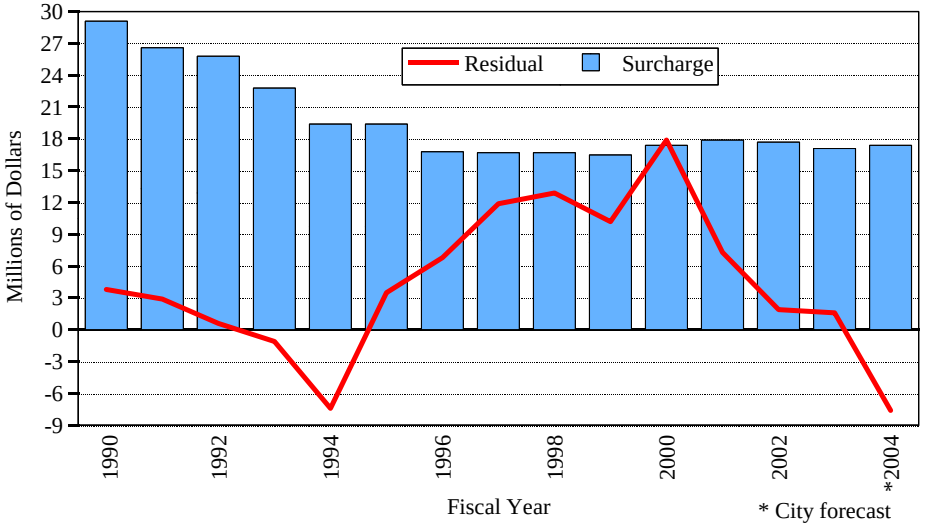
New York City's Off-Track Betting Corporation (OTB) was established by State law in 1970 as a public benefit corporation to operate a system of off-track betting parlors in New York City. It provides legalized pari-mutuel wagering that generates a stream of revenue for New York City, the State, and the horse racing and breeding industries.

OTB passes along to New York City the revenues from a mandated 5 percent surcharge on winning wagers, and its residual revenues.[33] Total distributions to New York City have declined from $32.9 million in FY 1990 to $18.7 million in FY 2003, which reflects a decline in both surcharge and residual revenues.

Despite handling about $800 million in wagers, OTB reported negative residual revenues, or losses, of $1.1 million in FY 1993 and $7.4 million in FY 1994 (see Graph 15). Residual revenues improved in subsequent years, peaking at $17.9 million in FY 2000, but have steadily declined since then and totaled only $1.6 million in FY 2003.

Graph 15

Residual and Surcharge Revenues



Sources: NYC Office of Management and Budget; NYC OTB; OSDC analysis

The OTB Financial Plan assumes that the loss to the City will be $7.6 million in FY 2004, the first loss in a decade. The projected loss is due to a number of factors, including State legislation that was enacted last year that requires OTB to pay an annual regulatory fee to the New York State Racing and Wagering Board for the right to simulcast thoroughbred racing at night. In addition, collective bargaining costs are projected to rise based on the agreement with District Council 37, and pension contributions continue to grow rapidly. According to OTB, New York City's share of

[33] Residual revenues represent the distribution to New York City after all operating expenses have been paid and all mandated distributions have been made to the racing industry, the State, and other localities. Residual revenues are frequently referred to as operating profits.

revenues for distribution has declined from 38 percent in FY 1988 to 19.5 percent in FY 2003 as a result of a series of State laws that have increased the distribution to the racing industry.

The OTB Plan projects small amounts of residual revenues during fiscal years 2005 through 2008 based on the assumption that operating costs will remain essentially unchanged during the plan period. To offset projected increases in personal service and lease costs, OTB intends to reduce staffing through attrition and hopes that the amounts wagered at OTB parlors will increase through a more targeted advertising campaign. However, OTB is likely to face increased competition for wagering dollars from the placement of video lottery terminals at Aqueduct Raceway and five other sites planned within New York City.

E. New York City Housing Authority

The New York City Housing Authority (NYHCA) provides affordable housing to nearly 420,000 low- and moderate-income City residents in 346 housing developments. According to NYCHA, it ended calendar years 2002 and 2003 with deficits of $74 million and $194 million, respectively. Moreover, NYCHA's January 2004 financial plan projected deficits of about $300 million for each of calendar years 2004 through 2007, which represents about 13.6 percent of revenues.

NYCHA intends to implement a series of cost-reduction and revenue-enhancement actions to balance the 2004 budget and narrow the projected deficits to $27 million in 2005 and to $15 million in each of calendar years 2006 and 2007. These actions include reductions in contracts ($69 million), supplies ($49 million), and equipment ($19 million), which could result in deferred maintenance. NYCHA also plans to reduce staffing levels by 686 employees during 2004 and by another 297 employees during 2005 for savings of $40 million in 2004 and about $65 million annually thereafter.

NYCHA also projects shortfalls in its capital budget, which is funded almost entirely by the federal government. NYCHA estimates that its capital needs will exceed available funding by $337 million during calendar years 2005 through 2007. Since the funding shortfall may require NYCHA to defer capital projects, it plans to implement a needs assessment process to prioritize capital projects. Despite the paucity of capital funds, NYCHA plans to use $74 million in federal capital funding to help balance its operating budget in 2004.

F. Municipal Assistance Corporation

In May 2003, the State Legislature passed legislation over the Governor's veto that would provide an annual $170 million payment to New York City through the Local Government Assistance Corporation (LGAC), with the understanding that these resources would be assigned by the City to a local development corporation (the Sales Tax Asset Receivable Corporation) that would refinance outstanding MAC bonds that date back to the 1970s fiscal crisis. While this transaction would benefit the City budget by $2.5 billion over the four-year period, the cost to the State would total $5.1 billion if the bonds were to be amortized over 30 years, as contemplated. The Comptroller believes that the refinancing is imprudent because it is costly, entails borrowing for operating budget purposes, and stretches out fiscal crisis debt that is due in less than five years.

The City had planned to complete the refinancing during FY 2004, but on August 13, 2003, the LGAC[34] filed a lawsuit challenging the constitutionality of the legislation and seeking to prevent the refinancing. The State Supreme Court granted the City's motion for summary judgment, but the plaintiffs appealed to the State Appellate Division, which had previously issued a preliminary injunction preventing the new local development corporation from issuing bonds pending appeal. Oral argument on the appeal took place on November 18, 2003, and on March 4, 2004, the State Appellate Division upheld the law. The LGAC again filed an appeal and oral arguments were heard on April 28, 2004.

On May 13, 2004, the Court of Appeals upheld the City's position that the legislation authorizing the $170 million transfer does not violate the State constitution. While LGAC has certified the payment, the State has not yet approved a new budget for the fiscal year that began on April 1, 2004. In addition, the emergency appropriation bills submitted by the Governor to the State Legislature have not included an appropriation for the $170 million. The Governor continues to propose alternatives that are intended to provide the same benefits to the City but at a far lower cost to the State.

The June Plan assumes that the refinancing will be completed during FY 2005 and that the City will still realize the benefits that had been anticipated during FY 2004. Thus, the June Plan anticipates debt service savings of $1 billion in FY 2005, including $502 million in savings that had been scheduled to be realized in FY 2004, and about $500 million in each of fiscal years 2006 through 2008.

[34] The State Comptroller is a director of the Local Government Assistance Corporation.

G. New York City Transitional Finance Authority

The New York City Transitional Finance Authority (TFA) has reached its legal issuing limit, and the Mayor and Governor have each proposed raising the limit. Both proposals would allow the City to issue TFA debt as long as the amount outstanding that exceeds the current cap of $11.5 billion, when combined with outstanding general obligation (GO) debt, does not exceed the City's constitutional debt limit.

The TFA was created in 1997 as the City was reaching its constitutional debt limit for GO bonds. To help the City meet its ongoing capital needs, the State authorized the TFA to issue debt backed by the City's personal income tax. TFA bonds have had the added benefit of coverage that is six times the covenanted maximum annual debt service. Because of this high coverage, TFA bonds have provided the City with interest cost savings. In addition, TFA bonds have provided a source of diversification as a financing vehicle, which relieves pressure on GO bonds and also lowers borrowing costs.

Currently, the City plans to issue $15.4 billion in general obligation bonds during fiscal years 2005 through 2008. If the TFA's debt issuing capacity were raised, City officials have stated that the City would use general obligation debt and TFA debt equally during the Financial Plan period to fund the City's capital program. If the City were able to issue TFA bonds in this manner, it would realize savings of about $23 million in interest expense during the Plan period because TFA interest rates have averaged about 17 basis points (one basis point is equal to one one-hundredth of a percent) lower than general obligation bonds in the secondary market.

The State also is considering legislation that would authorize the TFA to issue an additional $2.8 billion in debt above its legal limit to finance capital or operating needs that, in the judgment of the Mayor, are related to or arise from the distressed needs pertaining to educational facilities. The bill also would permit the TFA to securitize federal aid.

H. TSASC Inc.

In May 2003, Moody's Investor Service downgraded a major original participating manufacturer, R.J. Reynolds, to below investment grade, which triggered a "trapping event" in TSASC bonds. Bonds issued by TSASC are backed by revenues from the national settlement with tobacco companies. This trapping event requires TSASC to reserve a portion of the revenues until the total amount trapped equals 25 percent of the outstanding principal, which currently would total $1.3 billion. Unless the City takes actions to release the trapped funds, it is estimated that tobacco

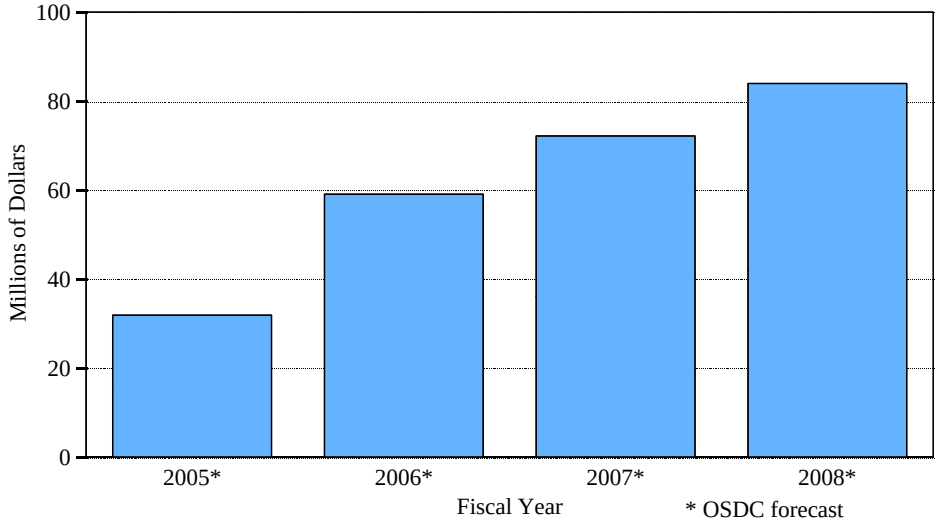
settlement revenues that would otherwise accrue to the City's budget would be reduced by $116 million in FY 2005 and about $60 million annually during fiscal years 2006 through 2008, for a total reduction of $296 million. City officials have stated that the City is considering options that would release the trapped funds, including restructuring outstanding TSASC bonds. Since recent events have made TSASC bonds more costly, the City no longer intends to fund a portion of its capital program with TSASC bond proceeds.

I. New York City Municipal Water Finance Authority

New York City leases its water and sewer systems to the Water Board, which sets user fees to reimburse the Municipal Water Finance Authority for the debt service on its bonds and to the City for costs associated with the operation and maintenance of the systems. In addition, the City has the right to request a rental payment from the Water Board of either the debt service on outstanding City general obligation debt issued for water and sewer purposes, or 15 percent of the debt service on outstanding water and sewer-related debt issued by the Municipal Water Finance Authority.

Graph 16

Additional Revenues Available to the City from Water and Sewer Fees



Sources: NYC Comptroller's Office; NYC Office of Management and Budget

In the past, the City collected rent based on outstanding general obligation bonds but, beginning in FY 2005, the City has requested that the Water Board

reimburse the City based on outstanding Municipal Water Finance Authority bonds. By using this methodology, the City will receive $32 million (about $9 per average bill) more than the cost related to the water and sewer system, which will be used to subsidize other municipal services. With outstanding authority debt projected to continue to increase to meet the growing capital needs of water and sewer systems, the spread between general obligation debt service and the authority's debt service will widen. As a result, the City will benefit by $59 million in FY 2006, $72 million in FY 2007, and $84 million in FY 2008 (see Graph 16). These additional funds will cost water and sewer rate payers an average of $18 in FY 2006, $21 in FY 2007, and $25 in FY 2008.

J. Hudson Yards Infrastructure Corporation

In February 2004, the Mayor announced an ambitious redevelopment plan to transform the far West Side of Manhattan into a high-density, mixed-use community. The plan has three major components: first, the renovation and expansion of the Jacob K. Javits Convention Center; second, the construction of a multi-use sports and convention facility, which would be used by the New York Jets and which is the centerpiece of the City's bid for the 2012 Olympics; and third, the extension of the No. 7 subway line and the creation of public spaces, such as parks. According to the City's 30-year plan, private developers will construct 14 high-rise office towers and more than 12,000 new housing units on the rezoned far West Side.

To finance the infrastructure improvements needed to encourage private investment on the far West Side, the Mayor would create the Hudson Yards Infrastructure Corporation (HYIC). HYIC would issue a total of $4 billion in bonds: $2.8 billion for the extension of the No. 7 subway line, a platform over the Metropolitan Transportation Authority's eastern rail yard, a new mid-avenue boulevard, and public amenities; another $1 billion to refinance short-term debt; and the remaining $200 million for bond-issuing expenses such as reserves and insurance. By creating a public benefit corporation, the Mayor has limited the involvement of the City Council and the City Comptroller, and circumvented the customary capital planning process.

The City projects that redevelopment of the far West Side will generate $16 billion in revenues to the City over a 30-year period that could be pledged to finance the infrastructure improvements. The projected revenues, which will be generated mainly by commercial payments-in-lieu-of-taxes (PILOTs) and residential property taxes, will be used to pay HYIC debt service. Because HYIC will incur debt service costs from the construction of the No. 7 subway line extension and other infrastructure improvements beginning in 2005, and development is not projected to

generate sufficient revenues to cover these costs until at least 2018, HYIC intends to issue short-term debt to pay interest costs not covered by revenues during the 13-year period. When revenues become sufficient to fund the debt service costs, HYIC would refinance an estimated $1 billion in short-term debt with long-term bonds. The City estimates that some of the bonds will be outstanding for as long as 40 years, with a total debt service cost of more than $10 billion.

Because there are no guarantees that revenues from future development will materialize in the magnitude expected or during the timeframe anticipated by the City, the City plans to use the Transitional Finance Authority (TFA),[35] with its high "AA" credit rating, to provide credit enhancement to HYIC's short-term debt. The amount of TFA liability (and by extension the amount of liability to the City) will depend on the total amount of short-term paper issued. Although no limit has been placed on the amount of short-term paper that could be backed by the TFA, the City intends to manage the program to limit the TFA's liability to $1 billion. The potential liability will also depend on the steps HYIC and the TFA take to respond to a revenue shortfall, and the nature and timing of such a shortfall.

HYIC bonds are expected to have a pledged revenue to debt service ratio of 1.5 to 1, which is lower than the TFA coverage ratio of 6 to 1. The financial community has reportedly expressed concerns about the HYIC financing plan in part because revenues, according to the City's own projections, would not begin to flow until at least 2010. Since bondholders would be relying on revenues from future development, HYIC's own underwriters and financial advisors have indicated that HYIC bonds would receive a low investment grade. Members of the financial community have suggested that the City take a more direct role in the financing of the far West Side redevelopment project to reduce the level of risk to potential investors.

In the event that the TFA is called upon to use its credit enhancement, City officials have indicated that the TFA would satisfy obligations from letters of credit from banks and ultimately purchase HYIC bonds, enabling HYIC to meet its debt service obligations. Such a purchase, however, would require amending the TFA's investment guidelines because the current guidelines only apply to funds held in reserve to meet TFA debt service payments and these guidelines only permit investment in higher rated bonds. To permit the TFA to purchase HYIC bonds, the TFA's five-member board[36] would have to revise their guidelines to permit such an

[35] The TFA is a public benefit corporation created by the State in 1997, when the City was approaching its State constitutional debt limit, to assist the City in funding its capital program.

[36] The board consists of the City Comptroller, the Speaker of the City Council, the City's Budget Director, the Commissioner of Finance, and the Commissioner of the Department of Design and Construction.

investment. The TFA has never before been used in this manner and such a purchase, if necessary, would create a hole in the City's budget because the revenues used for the purchase would have otherwise flowed to the City.

Although HYIC would be created as a legally separate entity from the City, HYIC bonds may be perceived by the financial community as a moral obligation of the City of New York and could adversely affect the City's credit rating. Also, we note that about half of the $4 billion in HYIC debt would be used to fund an extension of the No. 7 subway line, and that major transportation projects have a history of large cost overruns and delays. The City has suggested that the MTA would be responsible for any cost overruns, but the MTA has been adamant that the responsibility should remain with HYIC. In addition, the City's cost estimates exclude the $521 million cost of the second phase of redeveloping the far West Side, which includes a subway station at 41st Street and 11th Avenue and the northern portion of a mid-block boulevard running between 10th and 11th avenues—elements that are essential to the City's growth projections. Thus, the amount of bonds to be issued by HYIC, and hence the City's implicit liability, could exceed $4 billion.

K. New York Convention Center Development Corporation

To help finance the renovation and expansion of the Jacob K. Javits Convention Center, the Governor has introduced legislation that would expand the responsibilities of the Convention Center Development Corporation (CCDC), which would be authorized to issue $500 million in bonds that would be backed by a new $1.50 per night hotel room surcharge that the hotel industry has agreed to support. Another $200 million is expected to come from a private developer, and would help fund the $350 million cost of constructing a 1,500-room convention center hotel. In addition, the Governor has proposed that the CCDC be authorized to issue an unlimited amount of hotel bonds backed by future hotel revenues.

Concerns have been raised that the Governor's bill would implicitly authorize the construction and operation of a multi-use sports and convention facility before the public debate over the facility has concluded. The State Assembly recently introduced a bill that would separate the expansion of the Javits convention center from the construction and operation of a multi-use sports and convention facility. This would permit expansion of the Javits convention center to proceed while the debate over the multi-use facility continues.

On March 25, 2004, two Memorandums of Understanding (MOUs) were signed to advance the redevelopment of the far West Side of Manhattan. The first MOU, signed by the City and the State, included pledges by both entities to each

provide $350 million for the expansion and renovation of the Jacob K. Javits Convention Center and $300 million for the construction of a multi-use sports and convention facility.

The convention center would be renovated in two phases to provide additional meeting space and to be expanded north from 38th Street to 41st Street. When completed, the amount of space would double from 760,000 square feet to 1.5 million square feet, which would raise the convention center's ranking from 18th to fifth largest in the nation. The new multi-use sports and convention facility, which would have a retractable roof, would be built on a platform over the MTA's western rail yard. The facility is the centerpiece of the City's bid for the 2012 Olympics, and would also be home to the New York Jets beginning with the 2009 football season; would offer additional exhibition and meeting space; and could be reconfigured to create a plenary hall ranging from 5,000 to 45,000 seats.

The State and the City estimate that these projects would each cost $1.4 billion, but the estimate for the Javits expansion excludes the second phase of construction, which accounts for 35 percent of the total expansion. The public sector's contribution to the combined cost of $2.8 billion includes $1.8 billion to be generated from a new tax, the stretching out of existing debt, and the redirection of existing revenue streams to support new debt.

As shown in Table 9, the City plans to finance its $350 million contribution toward the first phase of the convention center project by securitizing certain surplus revenues of the Battery Park City Authority (BPCA). The use of these revenues requires the unanimous consent of the BPCA President, the Mayor, and the City Comptroller, who has not yet taken a position on the proposed use of these resources. The City plans to use $47 million on hand and plans to borrow the balance to meet its commitment to this project. Although the BPCA revenue stream is projected to decline from $29 million annually during fiscal years 2005 and 2006 to about $18 million annually beginning in FY 2008, the City has tightly structured the planned borrowing to reflect the projected revenue stream. The bill recently introduced by the State Assembly would prohibit the use of BPCA resources for this purpose and, if enacted into law, would require the City to identify an alternative funding source.

The State would finance its $350 million contribution by stretching out for another 30 years the remaining $268 million in outstanding convention center bonds that are due to be retired in 2012, and by issuing additional debt. The borrowing would be structured so that the debt service on the new bonds would be consistent

with the current State appropriation of $42 million for the existing convention bonds that would be refunded.

Table 9
Jacob K. Javits Convention Center
Renovation and Expansion Project
(in millions)

Cost of Construction	
Renovation and Expansion	$ 750
Convention Hotel	350
Other	300
Total	**$ 1,400**
Sources of Funding	
Hotel Tax	$ 500
BPCA Surplus Revenues	350
Debt Restructuring	350
Private Hotel Investment	200
Total	**$ 1,400**

Sources: Empire State Development Corporation; OSDC analysis

The second MOU, signed by the Empire State Development Corporation (ESDC), Jets Development LLC, and the MTA, outlines the financial responsibilities of each party involved in the construction of a multi-use sports and convention facility (see Table 10). The New York Jets would create a limited liability corporation to finance the construction of the facility, estimated at $800 million, which would be responsible for any cost overruns, including those associated with the construction of a platform over the western rail yard and a retractable roof. The City and State would each contribute $300 million to fund construction of the platform ($375 million) and the retractable roof ($225 million).

Table 10
Multi-Use Sports and Convention Facility
Sources of Funding
(in millions)

	New York Jets	New York State	New York City
Facility	$ 800	$ - - -	$ - - -
Rail Yard Platform	- - -	300	75
Retractable Roof	- - -	- - -	225
Total	**$ 800**	**$ 300**	**$ 300**

Sources: New York Jets; OSDC analysis

It has been widely reported that the State intends to create a local development corporation to issue $600 million in tax exempt bonds to finance a portion of the Jets' $800 million contribution, providing the Jets with interest savings of approximately $77 million. The debt service on the bonds would reportedly be funded with PILOTs that would otherwise flow into the City's coffers.

The City has not yet revealed the source of its $300 million contribution to the construction of the multi-use facility. Although the City expects to securitize an unidentified future revenue stream, it has not ruled out an income stream that currently benefits the City's budget.

It is expected that the MTA will be required to fund the debt service on bonds issued by a subsidiary or affiliate of the ESDC to fund the State's $300 million contribution, and that the State will not be under any contractual obligation to reimburse the MTA for these costs. The MTA has yet to negotiate an agreement with the New York Jets for the use of the platform, but there is no assurance that the ground lease payments would at least equal the debt service on the bonds. The MTA expects to obtain fair market value for the air rights over the rail yards and recently announced that it will seek an independent appraisal.

Ernst & Young conducted an economic impact study for the New York Jets and estimated that a multi-use facility would generate annual tax revenues of $72 million for the State and City, compared with debt service costs of $42 million on their $600 million contribution, which would generate a net profit of $30 million. ESDC reviewed the Ernst & Young study and concluded that the anticipated revenues would total $65 million. The New York City Independent Budget Office recently released a report that concluded that such a facility would generate annual tax revenues ranging between $19.6 million and $54.5 million, depending on usage. The actual profit generated by such a facility will ultimately depend on its use; the structure of the bonds used to finance the facility; the market conditions when the bonds are issued; and the extent that PILOTs, which would otherwise benefit the City, are used to fund the debt service on the bonds.

Appendix A

Nonrecurring Resources in Fiscal Year 2005

The June Plan includes $3.6 billion in nonrecurring resources in FY 2005 (see Table 11). These resources will help the City balance the FY 2005 budget, but will provide no recurring benefit.

Table 11
Nonrecurring and Other Extraordinary Actions
(in millions)

FY 2004 Surplus Transfer[37]	$ 1,700
Retroactive Port Authority Airport Lease Payment	687
MAC Refinancing	502
Debt Service Savings	169
Battery Park City Authority City Land Purchase	150
Pension COLA Stretch	96
Asset Sales	92
Tobacco Settlement Revenues	58
Anticipated Federal Aid	50
Other	68
Total	**$ 3,572**

Source: OSDC analysis

[37] The remaining $220 million of the FY 2004 surplus was transferred to FY 2006 to reduce the budget gap projected for that year.

Appendix B

City-Funded Staffing Levels
(Full-Time and Full-Time Equivalents)

Increase/(Decrease)

	Fiscal Year			Annual Change		Two-Year Change
	FY 2003	FY 2004	FY 2005	FY 2004	FY 2005	
Public Safety	**80,022**	**79,612**	**79,284**	**(410)**	**(328)**	**(738)**
Police Dept. Uniformed	36,120	34,774	34,774	(1,346)	- - -	(1,346)
Civilians	14,054	14,457	14,360	403	(97)	306
Fire Dept. Uniformed	10,879	11,104	11,154	225	50	275
Civilians	4,297	4,328	4,300	31	(28)	3
Correction Uniformed	8,786	8,772	8,740	(14)	(32)	(46)
Civilians	1,323	1,405	1,375	82	(30)	52
District Attys. & Prosecutors	3,412	3,376	3,263	(36)	(113)	(149)
Probation Department	763	977	917	214	(60)	154
Other	388	419	401	31	(18)	13
Health and Welfare	**21,837**	**23,714**	**24,902**	**1,877**	**1,188**	**3,065**
Social Services	9,062	10,575	11,208	1,513	633	2,146
Children's Services	6,380	6,481	6,522	101	41	142
Health and Mental Hygiene	4,006	4,298	4,722	292	424	716
Homeless Services	2,109	2,096	2,256	(13)	160	147
Other	280	264	194	(16)	(70)	(86)
Environment & Infrastructure	**16,563**	**16,933**	**16,812**	**370**	**(121)**	**249**
Sanitation Uniformed	7,006	7,525	7,630	519	105	624
Civilians	1,751	1,818	1,839	67	21	88
Dept. of Transportation	2,035	2,084	2,154	49	70	119
Parks & Recreation	5,373	5,078	4,749	(295)	(329)	(624)
Other	398	428	440	30	12	42
General Government	**8,041**	**8,767**	**9,004**	**726**	**237**	**963**
Finance	2,166	2,415	2,401	249	(14)	235
Law Department	1,285	1,290	1,295	5	5	10
Citywide Admin. Services	1,346	1,428	1,583	82	155	237
Taxi & Limo. Commission	447	479	472	32	(7)	25
Investigations	269	279	271	10	(8)	2
Board of Elections	373	328	344	(45)	16	(29)
Info. Technology & Telecomm.	552	817	864	265	47	312
Other	1,603	1,731	1,774	128	43	171
Housing	**1,399**	**1,492**	**1,849**	**93**	**357**	**450**
Buildings	893	915	943	22	28	50
Housing Preservation	506	577	906	71	329	400
Department of Education	**110,435**	**113,138**	**112,665**	**2,703**	**(473)**	**2,230**
Pedagogues	90,049	91,376	91,095	1,327	(281)	1,046
Non-Pedagogues	20,386	21,762	21,570	1,376	(192)	1,184
City University of New York	**6,033**	**6,185**	**6,090**	**152**	**(95)**	**57**
Pedagogues	3,674	3,912	3,918	238	6	244
Non-Pedagogues	2,359	2,273	2,172	(86)	(101)	(187)
Elected Officials	**2,446**	**2,604**	**2,555**	**158**	**(49)**	**109**
Total	**246,776**	**252,445**	**253,161**	**5,669**	**716**	**6,385**

Sources: NYC Office of Management and Budget; OSDC analysis

Major contributors to this report include:

Kenneth B. Bleiwas	Deputy Comptroller for the City of New York
Roger Liwer	Assistant Comptroller
Adam Freed	Director, Bureau of Economic Development and Public Policy
Michael Solomon	Director, Bureau of Agency Analysis
Michael Brisson	Deputy Director, Bureau of Tax and Economic Analysis
Jane Moore	Report Editor

Steven Brooks
James Chen
Mark Chernoff
Diane Diamond
Robert Horowitz
Bob Kepple
Leonard Liberto
Cheryl Pahaham
Arfan Putra
Sandy Stevenson